

***United States Court of Appeals
for the Second Circuit***



**BRIEF FOR
APPELLANT**

Original with Proof of Service

76-7406

To be argued by
REGINALD LEO DUFF

United States Court of Appeals

FOR THE SECOND CIRCUIT

MAXIME C. BARETGE; ROCKLEY ASSOCIATES, S.A.; PIERRE
MACHERAS; DAVID W. TRIMBLE; THE ROCKLEY GROUP,
INC.; LA BAZOCHE, INC.; WALBORG CORPORATION; and
COBLENTZ BAG CO., INC.,

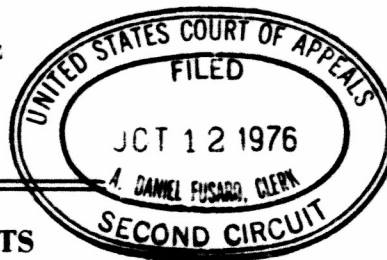
Plaintiffs-Appellants,

—against—

NORMAN N. BARNETT, JULIENNE BARNETT,
and VI L. MESSERLI,

Defendants-Appellees.

APPEAL FROM A JUDGMENT AND ORDER OF THE
UNITED STATES DISTRICT COURT FOR THE
SOUTHERN DISTRICT OF NEW YORK



**BRIEF OF THE PLAINTIFFS-APPELLANTS
AND APPENDIX**

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-against-

NORMAN N. BARNETT, JULIENNE BARNETT,
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Defendants-Appellees.

BRIEF OF THE PLAINTIFFS-APPELLANTS

Plaintiffs-Appellants ("plaintiffs") appeal from a judgment (A-2),* entered upon an unpublished memorandum decision (A-3) of the United States District Court for the Southern District of New York, Hon. Charles L. Brieant, U.S.D.J., dismissing their complaint for lack of jurisdiction of the subject matter and for failure to state a claim for which relief can be granted under Rule 10b-5, 17 CFR § 240.10b-5. Although the motion to dismiss had been made only by the two served defendants, Norman N. Barnett ("Barnett") and his wife, Julianne Barnett ("Julienne"), Judge Brieant dismissed as to all three named defendants.

THE MOTION TO DISMISS AND THE DECISION BELOW

The Barnetts moved below on a naked notice of motion (A-4-5) to dismiss the complaint on two alternative grounds:

*References preceded by "A" are to the Appendix, which contains the entire operative Record below (exclusive of stipulations and memoranda of law).

(1) That the Court lacked jurisdiction of the subject matter because the complaint only alleged corporate mismanagement and failed to state a claim under Rule 10b-5;* and (2) That the complaint did not set forth the alleged frauds with the particularity required by Rule 9(b) of the Federal Rules of Civil Procedure. The parties joined issue on these grounds, plaintiffs primarily relying upon this Court's decision in Schlick v. Penn-Dixie Cement Corp., 507 F.2d 374, 379-80, 378-79 (2d Cir. 1974), as to both branches of defendants' motion.

The Court below dismissed the complaint with a memorandum endorsement (A-3) which went off on a wholly different ground: It held that Counts I and II failed to state a claim under the Exchange Act because "defendants . . . were [not] 'sellers' of securities in violation of Rule 10b-5; nor were plaintiffs buyers thereof from defendants." The Court below cited no authority for its novel requirement that the plaintiff be a purchaser from the defendant. No such authority exists.

Moreover, in referring only to Counts I and II of the complaint, the Court evidently overlooked the fact that Count IV explicitly alleges that in March 1976 defendant Barnett sold his stock in Rockley to the individual plaintiffs, and that as part of the consideration therefor each of the plaintiffs was required to give general releases running to Barnett and his wife, defend-

*Where jurisdiction is based solely upon the Exchange Act and the complaint fails to state a claim thereunder, the dismissal is properly one for lack of jurisdiction of the subject matter. Fershtman v. Schectman, 450 F.2d 1357, 1361 (2d Cir. 1971).

ant Julianne. In wholly ignoring Count IV, the Court below evidently relied more upon defendants' characterization of that Count as a pendent claim (Memo. below, p. 5) than upon the allegations of that Count itself.

Similarly, in dismissing Counts I and II, the Court failed to consider the alternative jurisdictional allegation that as to those two counts there is complete diversity of citizenship between the individual plaintiffs and defendant Barnett, and the requisite jurisdictional amount (A-6, ¶ 1).

THE FRAUDULENT SCHEME

Defendant Barnett's fraudulent scheme involves a three-step progression: (a) His acquisition of control of a corporate complex with plaintiffs' money and by means of the sale of securities; (b) his looting of the corporations so acquired; and (c) his inducing plaintiffs to purchase additional securities, followed, in the face of foreclosure and bankruptcy, by his resale of his fraudulently acquired controlling stock to the individual plaintiffs for various considerations, including general releases.

It is alleged that Barnett's wife Julianne and defendant Messerli conspired with, and aided and abetted Barnett's violations of Rule 10b-5, and were themselves recipients of moneys and other property fraudulently obtained from the individual plaintiffs either directly, or through the corporate treasuries into which the individual plaintiffs had been induced to invest their funds.

Had Barnett simply taken the individual plaintiffs' subscription money and run, or had he sold them stock in a worthless shell corporation, the violation of Rule 10b-5 would be clear. It is no less clear that Rule 10b-5 is the operative provision and that Barnett's acts violate it because, for a period of some eighteen months, Barnett filtered plaintiffs' money by having them invest it in the corporate plaintiffs, and enriched himself with funds stolen from the corporate treasuries rather than directly from plaintiffs.

Thus this action is not one in which the primary wrong is corporate mismanagement or breach of fiduciary duty, with only a peripheral sale of stock. Without the purchases and sales of securities there would have been no corporations for Barnett to loot. The acquisition of Walborg Corporation ("Walborg") was the object of the individual plaintiffs' initial investments, and the other corporate plaintiffs were created to hold the stock of Walborg and plaintiffs' subscriptions, and as a means of inducing the investments by plaintiffs which Barnett subsequently embezzled with the active assistance and participation of his wife (a director of Walborg) and Messerli (a de facto officer of Walborg).

THE ALLEGATIONS OF THE COMPLAINT

The complaint is in four Counts. Counts I, II and IV purport to allege violations of Rule 10b-5. Count III, alleges corporate waste and looting and is pendent to Counts II and IV. The acts complained of in Count III are among the material facts disclosure of which is claimed to have been omitted by Barnett in

connection with the sales of securities complained of in Counts II and IV of the complaint.

Count I

The action arises out of the acquisition of an operating company in 1974 by several foreign investors, the "individual" plaintiffs Baretge, Macheras, Trimble and Rockley Associates, S.A. Count I of the complaint, which is brought by the individual plaintiffs solely against Barnett, alleges (A-10-11, ¶¶ 11-13) that said plaintiffs, acting through Baretge, agreed with Barnett to have him find a suitable investment in the high fashion consumer importing business with a view to an eventual public offering of its securities if it proved successful. Barnett was to manage the enterprise for the individual plaintiffs.

Barnett learned of the availability for sale of the stock of Walborg, an importer of women's handbags, and negotiated with its owners to acquire its stock on behalf of a corporate nominee. The actual acquisition of Walborg's stock was made by him in the name of a newly formed New York corporation, La Bazoche, Inc. ("La Bazoche") (A-11-12, ¶ 15),* all of the stock of which was issued to another newly formed Delaware corporation, Rockley Group, Inc. ("Rockley"), in which the individual plaintiffs and Barnett became investors by purchasing its stock. However, Barnett arranged to make himself the sole voting trustee of the stock of La Bazoche and its sole director.

* "La bazoche" means "handbag" in French.

Count I of the complaint alleges that in connection with the purchase of the stock of Walborg and the sale of the stock of Rockley to the individual plaintiffs, Barnett made at least two material misrepresentations of fact:

(a) He falsely represented to the sellers of Walborg's stock ("the Weinbergs") that he was the sole voting trustee of La Bazoche (although it had not yet been formed), and that his sole voting rights over its stock was the Weinbergs' best protection (since part of the purchase price for their Walborg stock was to be paid out over a period of time) (A-13-14, ¶ 17(a)); and

(b) To the purchasers of Rockley's stock (the individual plaintiffs) he falsely represented that the Weinbergs themselves had insisted, as a condition for selling their Walborg stock, that Barnett have the sole voting power over the stock of La Bazoche (through the voting trust agreement) in order to assure the Weinbergs that La Bazoche would honor its obligations to them (A-14, ¶ 17(b)).

Count I alleges that the creation of a wholly unnecessary corporation (La Bazoche) between the operating subsidiary (Walborg) and the holding company (Rockley) owned by the individual plaintiffs was a manipulative device and an indispensable part of Barnett's fraudulent scheme (A-14-15, ¶ 18), and that he falsely represented to the individual plaintiffs that its incorporation was necessary to provide them with limited liability (ibid.).

Count I also alleges that in connection with the first purchase and sale of securities Barnett falsely represented to

the individual plaintiffs the value of his own contribution to Rockley---crediting himself with the full value of La Bazoche's stock (although its sole asset, the stock of Walborg, had been acquired in part with funds of plaintiff Baretge, and in part by bank loans payable by La Bazoche (and secured by Barnett's worthless guarantees), and with the purported transfer to Rockley of cash and stock in another corporation (Belmont Industries, Inc.) which Barnett never in fact acquired or transferred to Rockley---with the result that Barnett became the majority shareholder of Rockley for no cash investment of his own (A-15-17, ¶¶ 20-21).

It is alleged that Barnett also made misrepresentations to the individual plaintiffs concerning the manner in which he would conduct the business of the companies (A-14-15, A-17, ¶¶ 18, 19, 22), that the representations were known by him to be false (A-17, ¶ 22), that the individual plaintiffs did not and could not know of the falsity of those representations (A-17-18, ¶ 23), and had they known the true facts they would not have invested their funds in Rockley or purchased its stock (A-19, ¶ 25).

Count II

Count II, which is also brought by three of the individual plaintiffs, solely against Barnett, alleges (A-20, ¶ 28) that in December 1975 Barnett induced the individual plaintiffs Baretge, Rockley Associates, S.A., and Trimble to purchase additional stock of Rockley for \$187,500 (A-21, ¶ 30):

(a) By falsely representing to them that while the financial condition of Rockley and its subsidiaries was

sound, the banks which had lent La Bazoche much of the funds used to acquire the stock of Walborg and another operating subsidiary (Coblentz), were concerned with Rockley's high debt-to-equity ratio and desired investment of additional equity funds to reduce that ratio (ibid.);

(b) In response to the individual plaintiffs' repeated requests for current financial statements for Rockley and its subsidiaries, by falsely representing to the individual plaintiffs that the financial statements of Rockley and its subsidiaries were not available because of problems with the computer (whereas they were in fact available)(A-20, ¶ 27);

(c) By failing to inform the individual plaintiffs that Rockley and its subsidiaries were on the verge of insolvency and could not pay their debts (A-21, ¶ 31), and

(d) By failing to inform the individual plaintiffs that any additional funds which they invested in Rockley would be appropriated by Barnett and his wife, defendant Julianne, and by their co-conspirator, defendant Messerli (A-21, ¶ 31).

It is alleged (A-20-21, ¶¶ 29-30) that the representations by Barnett were knowingly false when made, were relied on by the individual plaintiffs (A-21, ¶ 32), and that Barnett misappropriated the funds invested by them (A-21, ¶ 31).

Count IV

Count IV (A-28-30), which is brought by all plaintiffs against Barnett, his wife Julianne and their co-conspirator, Messerli, alleges that on or about March 29, 1976, Barnett resigned

from all of his positions with Rockley and its subsidiaries, sold his stock therein to the individual plaintiffs, obtaining as part of the purchase price therefor general releases from each of the plaintiffs running to himself and his wife, defendant Julianne; a Mercedes Benz automobile; and a promise by Walborg to pay him \$60,000 over nine months.

Count IV alleges (A-28-30, ¶¶ 42-44) that in selling his said stock to the individual plaintiffs, Barnett not merely omitted to inform them that he had looted Rockley and its subsidiaries of valuable assets and moneys, as set forth below, but that he withheld such information, by keeping the corporate books and records at his home rather than at the corporate offices, and by ordering two of the individual plaintiffs (Baretge and Trimble) from Walborg's premises although they were directors of its grandparent corporation, Rockley, and principal stockholders and beneficial owners of the overall enterprise.

The self-dealing acts which were not disclosed to the plaintiffs which are alleged with particularity in Count III of the complaint and incorporated by reference into Count IV, included:

(a) Barnett's making of unsecured loans aggregating \$45,000 to himself from corporate funds of one or more of the corporate plaintiffs in 1975 and 1976, without the knowledge or approval of Rockley's board of directors (A-23-24, ¶ 34(c)(j));

(b) Barnett's making of unsecured loans aggregating \$20,000 to defendant Messerli from corporate funds of Rockley

and Walborg, and his purported cancellation of the notes evidencing such loans in January 1976, after the additional investments alleged in Count II, in each case without the knowledge or authorization of Rockley's board of directors* (A-25-26, ¶ 34(m));

(c) Barnett's making unauthorized payments of \$8,000 to his wife, Julianne, in January or February 1976, while she was a director of Walborg and after the new investments alleged in Count II (A-18, ¶ 34(e));

(d) Barnett's incurring approximately \$400,000 in "expenses" during 1974 and 1975 (A-22-23, ¶¶ 34(a), (b), (d), (f));

(e) Barnett's conversion of the cash value, worth approximately \$106,000, of a "key man" life insurance policy on the lives of the Weinbergs, the original vendors of Walborg, to whom La Bazoche still owed part of the purchase price for the Walborg stock (¶ 34(h));

(f) With the complicity of defendant Messerli, Barnett's embezzlement on or about February 26, 1976 (shortly after the new investments alleged in Count II, and days before he commenced negotiations with the individual plaintiffs for the sale of securities alleged in Count IV) of a "key man" life insurance policy on his own life owned by Walborg and having a

*Since the filing of the complaint below, Barnett submitted affidavits in Messerli's state court action against some of the plaintiffs (see post, pp. 12-13), alleging that the purported cancellation of Messerli's \$20,000 note payable to Rockley had been approved by Walborg's board of directors. Since these are public records, this Court may properly note them. If desired or necessary, plaintiffs will hand up substantiating excerpts.

cash surrender value of approximately \$33,000, ownership of which Barnett purported immediately to transfer to his wife, defendant Julianne (¶ 34(k)), who thereupon attempted to appropriate its cash value for her own uses.*

Count III

Count III, which is pendent to the other Counts, particularly Counts II and IV, is brought by the corporate plaintiffs against all three defendants, and particularizes the various thefts and diversions of corporate properties of the four companies, Rockley, La Bazoche, Walborg, and Coblentz Bag Co., Inc. Its allegations are incorporated by reference into Count IV, and thus provide the particularization as to the matters which Barnett fraudulently failed to disclose in alleged violation of Rule 10b-5, in connection with his sale of Rockley stock to the individual plaintiffs in exchange for various considerations to himself and his wife, defendant Julianne, including general releases of unspecified and undisclosed wrongdoing.

Plaintiffs contend that proof of the alleged misrepresentations and omissions, particularly those alleged in Counts II and IV, while requiring the additional proof of the non-disclosure,

*When this action was instituted plaintiffs lacked documentation even of which corporation owned the policy. In their suit against the insurance company it has been disclosed that Barnett, with Messerli's co-signature, purported to transfer ownership to himself on February 26, 1976, and on the following day transferred ownership to Julianne, who immediately made herself the beneficiary. Thereafter Julianne directed the application of the loan value to payment of the following year's premium (which the pendency of that action prevented), which would have left Walborg liable for \$24,000 on account of a prior premium finance loan.

will simultaneously prove the allegations of corporate waste, breach of fiduciary duties and misappropriation of corporate assets alleged in Count III, so that Count III is properly pendent to those counts. United Mine Workers v. Gibbs, 383 U.S. 715, 726 (1966).

The complaint seeks (A-30-34) an accounting and damages, a declaration of the invalidity of the general releases extorted from the several plaintiffs (since plaintiffs had never been informed of what they were being asked to release (A-29-30, ¶¶ 43-44)), and the rescission of Walborg's promise to pay Barnett \$60,000.

OTHER ACTIONS

As we have noted above, in addition to the present action there are two other civil actions involving the plaintiffs and the defendants. On April 30, 1976, defendant Messerli instituted an action in the Supreme Court, New York County, Messerli v. Rockley Group, et al., N.Y. County Index No. 7715/1976, seeking an injunction, compensatory and punitive damages, claiming that she was an employee for a term and had been wrongfully discharged by Rockley. In her motion she was supported by affidavits submitted by Barnett.

The defendants therein (the corporate plaintiffs below) immediately counterclaimed to recover from Messerli \$20,000 in unauthorized corporate loans to Messerli which Barnett had purported to cancel, and an accounting and damages, including those resulting from her co-signing the purported assignment to Barnett

of Walborg's insurance policy on Barnett's life, and they sought an order of attachment or similar relief.

Special Term denied Messerli's motion for injunctive relief and struck her prayer for punitive damages, but denied the cross-motions of the defendants therein (the corporate plaintiffs herein) for an attachment or similar relief and their motion for summary judgment. Cross-appeals are now pending to the Appellate Division of the Supreme Court.

On May 3, 1976, simultaneously with the filing of the complaint herein, some of the present corporate plaintiffs (initially Rockley and La Bazoche, joined by Walborg in an amended complaint) instituted an action against the Equitable Life Insurance Company of Iowa, for a declaratory judgment that they or one of them remains the true owner and beneficiary of the life insurance policy on the life of Barnett which he had embezzled (with Messerli's co-signature) and thereafter transferred to his wife, Julianne, and seeking recovery of its cash surrender value. That action, also pending in the Southern District of New York, The Rockley Group, Inc., et al. v. Equitable Life Insurance Company of Iowa, 76 Civ. 1993, is assigned to Hon. Inzer B. Wyatt, U.S.D.J. The insurance company has interpleaded the Barnetts and the plaintiffs therein, and there is now pending before Judge Wyatt the Barnetts' motion to dismiss the complaint and the counterclaim in interpleader for lack of subject matter jurisdiction.

QUESTIONS PRESENTED

1. May a claim under Rule 10b-5 be maintained by the purchaser of securities against a party who was not the owner of the securities sold in violation of the Rule, but who participated in the sale and induced the purchase of the securities by the plaintiff? The Court below held that it may not, evidently overlooking the allegation of Count IV, that defendant Barnett sold his own securities in Rockley Group to the individual plaintiffs.

2. Is the complaint below jurisdictionally deficient in allegedly pleading merely a claim of corporate waste or mismanagement, as is claimed in defendants' motion to dismiss? The Court below did not reach this ground for dismissal urged by defendants below.

3. Was the complaint sufficiently particular in its specifications of fraud to comply with the requirements of Rule 9(b) of the Federal Rules of Civil Procedure? The Court below did not reach this ground for dismissal urged by defendants below.

4. Does Count IV of the complaint state a claim under Rule 10b-5 against defendants Julianne Barnett and Vi L. Messerli on account of their aiding and abetting Barnett's violations of Rule 10b-5, and their receiving moneys obtained from the sale of securities to plaintiffs, and other valuable considerations given by plaintiffs for the sale of securities, as alleged in Count IV with respect to defendant Julianne Barnett, or because of their

aiding and abetting of defendant Barnett's violations of Rule 10b-5, either as aiders and abettors of or as conspirators with Barnett, or on principles of pendent jurisdiction of the person? Without consideration the allegations of Count IV, the Court below implicitly held that it does not.

5. Is Count III of the complaint properly pendent to some or all of the other counts? The Court below did not consider whether said Count was pendent since it held that there was no valid federal claim to which it could properly be pendent.

6. Did the Court below have jurisdiction of Counts I and II by reason of the diversity of citizenship of the parties and jurisdictional amount? The Court below did not discuss the jurisdiction based upon diversity of citizenship.

POINT I

THE COURT BELOW APPLIED IMPROPER STANDARDS, AND IGNORED THE WELL-PLEADED ALLEGATIONS OF THE COMPLAINT IN HOLDING THAT PLAINTIFFS LACK STANDING TO SUE UNDER RULE 10b-5, OR THAT DEFENDANTS MAY NOT BE SUED THEREUNDER

As we have stated in our introductory statement, the District Court dismissed the complaint herein not on either of the grounds upon which the motion to dismiss had been made by the defendants, but upon a ground which had not been advanced: namely that the complaint failed to allege that the defendants were sellers of securities, and that the plaintiffs were buyers thereof from defendants.

While a District Court unquestionably has the power and duty to dismiss a complaint for lack of subject matter jurisdiction even on a ground not urged upon the Court, Rule 12(h)(3), plaintiffs respectfully submit that in dismissing the complaint below Judge Brieant not merely misread the allegations of the complaint actually before him, but imported into Rule 10b-5 a condition to suit which has never heretofore been imposed by any court, which is contrary to such decisions as have considered the question. In such circumstances the Court might profitably have solicited briefs to guide his decision.

Because it is short, we quote the District Court's decision in its entirety (A-3):

"A careful reading of this complaint shows with respect to Counts I and II that neither the moving defendants nor Messerli were 'sellers' of securities in violation of Rule 10b-5; nor were plaintiffs buyers

thereof from defendants. However, the pleading be characterized or described, it fails to state a claim under §10b of the 1934 Act in either of these counts. Blue Chip Stamps v. Manor Drugstores, 421 U.S. 732 (1975). Even before Blue Chip we had been cautioned more than once against 'a trend we have observed with disturbing frequency, namely, invocation of the salutary anti-fraud provisions of the federal securities laws in cases where those provisions are wholly inappropriate and wide of the Congressional mark.' [Quoted from Kavit v. A. L. Stamm & Co., 491 F.2d 1176 (2d Cir. 1974), relying in turn on Ryan v. J. Walter Thompson Co., 453 F.2d 444, 445 (2d Cir. 1971)].

"Under the circumstances, there is no basis to exercise pendent jurisdiction.

"Motion granted. Complaint dismissed as to all defendants, including Messerli."

- (a) The Court below misconstrued a rule governing plaintiff's standing to sue under Rule 10b-5 as a limitation on who may be a defendant in suits brought under that Rule

The decision below is insupportable. Neither Blue Chip Stamps nor any other decision known to plaintiffs imposes a requirement that the plaintiff be a purchaser from the defendant. Blue Chip, like Birnbaum v. Newport Steel Corp., 193 F.2d 461 (2d Cir. 1952), which first enunciated the "purchaser-seller" requirement, and Birnbaum's progeny, relate only to the standing of the plaintiff, and require that a plaintiff in a suit under Rule 10b-5 be either a purchaser or a seller of a security, and not merely someone who would (or might) have bought (or sold) had the facts been disclosed.

Judge Brieant misreads Blue Chip as restricting the character of the defendant who may be named in a Rule 10b-5 action, apparently requiring that he be the prior owner of the security

sold. Facially this is not a "standing" rule, but one which exempts from the coverage of Rule 10b-5 numerous categories of person who fraudulently induce purchases of securities from others, and have routinely been held to be proper Rule 10b-5 defendants. The new rule enunciated below neither flows from the text of Rule 10b-5 nor is supported by any reason of policy.

Apart from cases like Shapiro v. Merrill Lynch, 495 F.2d 228 (2d Cir. 1974), which impose liability for trading on inside information without regard to any privity between the plaintiff's purchase and the defendant's sale, the cases are legion which hold liable under Rule 10b-5 persons whose "conduct has amounted to solicitation of the sale." E.g., Katz v. Amos Treat & Co., 411 F.2d 1046 (2d Cir. 1969) (non-owner broker-dealer and its registered representative, attorney for the issuer); Moerman v. Zipco, Inc., 302 F.Supp. 439 (E.D.N.Y. 1969), aff'd. on opin. below, 422 F.2d 871 (2d Cir. 1970), rehearing denied, 430 F.2d 362 (2d Cir. 1970) (director who induced the sale); DeMarco v. Edens, 390 F.2d 836 (2d Cir. 1968) (underwriter; quaere whether underwriter was "owner" or not); Myzel v. Fields, 386 F.2d 718, 739 (8th Cir. 1967) (agent, financial adviser with knowledge, and controlling person); cf., Globus v. Law Research Service, Inc., 418 F.2d 1276 (2d Cir. 1969) (holding both issuer and underwriter in private placement liable, where only one could be the "seller"); Herzfeld v. Laventhol, Krekstein, Horwath & Horwath, ____ F.2d ____, CCH Sec.L.Rep. ¶ 95,660, at p. 90,260 (2d Cir. 1976) (liability of accountant); compare, Hochfelder v. Ernst & Ernst, 503 F.2d 1100

(7th Cir. 1974), rev'd. on other grounds, Ernst & Ernst v. Hochfelder, ___ U.S. ___, 47 L.ed.2d 668 (1976) (accountant).

Even under section 12 of the Securities Act, 15 U.S.C. § 771, in which the right of action is explicitly given to a purchaser of securities against his "seller," it has been recognized that the term "seller" may include someone other than the prior owner of the security. Value Line Fund, Inc. v. Marcus, CCH Sec.L.Rep. ¶ 91,523 (S.D.N.Y. 1965). The Court in Nicewarner v. Bleavins, 244 F.Supp. 261, 266 (D. Colo. 1965), recognized the principle while finding that the defendant there did not come under it on the facts:

"It is well established that persons other than the owner of a security may be liable under 12(1). See Loss, Securities Regulation, Ch. 11C(d)(i), pp. 1712-1719. Such persons include brokers or other agents for the seller, and directors, officers, or controlling persons of a corporation. However, in all instances where a non-owner has been held liable his conduct has amounted to solicitation of the sale. These decisions simply recognize that a person may sell what he does not own. This imports a causation requirement into section 12(1): 'But for' this person's conduct, there would have been no sale. In the present case, while it appears that the sale would not have been consummated without the services of some attorney, the evidence fails to establish that Hudson did more than serve as an attorney." (Emphasis added).

Rule 10b-5 by its terms contains no restriction similar to that found in section 12, but premises liability upon misrepresentations or material omissions or other fraudulent devices or contrivances occurring "in connection with the purchase or sale of any security." This is language far too broad to be restricted to limiting liability only to owner-sellers, and, as noted above, the reported decisions have never so limited it until now.

The decision below is wholly untenable because, on its rationale, a subscriber to the stock of a newly formed corporation could never maintain an action under Rule 10b-5 against the corporation's promoters since, by hypothesis, the stock would have been issued by the corporation and the promoter would not be the "seller" in the sense apparently used by the Court below. Nor are we being either hypothetical or hyperbolic: Count I of the complaint essentially alleges that state of facts (despite defendants' efforts in the pre-argument conference to distinguish Barnett's role from that of a conventional promoter by observing that both he and the individual plaintiffs invested in the new corporation), since Barnett structured the transaction and gave himself a controlling interest in Rockley at no cost to himself.

(b) The Court below applied
improper standards in
dismissing the complaint

Quite apart from the District Court's patent misreading of Blue Chip to impose an untenable precondition to Rule 10b-5 liability, the District Court's decision manifestly violates this Court's admonition against dismissal on naked notices of motion of actions brought under the Exchange Act and particularly under Rule 10b-5. As this Court said in A. T. Brod & Co. v. Perlow, 375 F.2d 393, 397 (2d Cir. 1967):

"Nor do we think it sound to dismiss a complaint merely because the alleged scheme does not involve the type of fraud that is 'usually associated with the sale or purchase of securities'. We believe that § 10(b) and Rule 10b-5 prohibit all fraudulent schemes in connection with the purchase or sale of securities, whether the artifices employed involve a garden type

variety of fraud, or present a unique form of deception. Novel or atypical methods should not provide immunity from the securities laws." (Emphasis in text).

And see, Superintendent of Insurance v. Bankers Life & Cas. Co., 404 U.S. 6 (1971).

The Court below purported to find support for its dismissal of the complaint in Kavit v. A. L. Stamm & Co., 491 F.2d 1176 (2d Cir. 1974), and Ryan v. J. Walter Thompson Co., 453 F.2d 444 (2d Cir. 1971). However, neither of those decisions supports the dismissal on a naked motion to dismiss, nor sustains the dismissal on facts comparable to those in the case at Bar. Kavit was a judgment for defendant rendered after trial, although this Court indicated that an interlocutory appeal from an earlier refusal to stay arbitration* might have found a sympathetic audience. Similarly, in Ryan the plaintiff was legally bound to resell his stock to defendant, so that no putative omission could have been "material." Accordingly, this Court held that the granting of summary judgment was appropriate.

In contrast, the motion below was a naked motion to dismiss. On such a motion the District Court may not dismiss a complaint merely because the allegations of fraud have not yet been proven, as this Court observed in the Brod case, supra, 375 F.2d at 398:

*The fact that arbitration was involved itself imports considerations wholly lacking in the present case, as this Court observed in Pearlstein v. Scudder & German, 429 F.2d 1136, 1143 (2d Cir. 1970), quoted post, p. 31.

"It is true, of course, as the Perlows submit, that Brod has not proven that the Perlows' failure to make payment constituted a 'device, scheme or artifice to defraud. . . .' But, whether there is actionable fraud or a mere breach of contract depends on the facts and circumstances developed at the trial or on motion for summary judgment. Brod was not required to prove in its complaint that it was entitled to an ultimate recovery, nor was it required to set forth in its complaint a detailed statement of the facts. . . . Such simplified 'notice pleading' requires that the complaint be construed liberally . . . and 'jurisdiction * * * is not defeated * * * by the possibility that the averments might fail to state a cause of action on which * * * [the pleader] could actually recover. . . .'

". . . But, accepting Brod's allegation as true, as we have indicated we must on a motion to dismiss the complaint, it is clear that the complaint sufficiently stated a claim grounded in federal jurisdiction. The order and judgment of the District Court dismissing the complaint for lack of subject matter jurisdiction must, therefore, be vacated and reversed." (Emphasis in text).

Patently the complaint should not have been dismissed on a naked notice of motion if plaintiffs can prove any state of facts which would entitle them to relief. Shell v. Hensley, 430 F.2d 819, 826 (5th Cir. 1970). We submit and expect to demonstrate that the complaint in suit permits plaintiffs to do just that. The order and judgment below, dismissing the complaint, s d therefore be reversed.

POINT II

THE COMPLAINT SUFFICIENTLY
ALLEGES VIOLATIONS OF RULE
10b-5 TO WITHSTAND DEFEND-
ANTS' MOTION TO DISMISS

As we have heretofore noted, the motion to dismiss actually made by defendants differed substantially from the ratio decidendi of the Court below. Nevertheless, the grounds urged for dismissal below also were legally insufficient, and will not support the order and judgment of dismissal being appealed herein.

- (a) The complaint was not jurisdictionally deficient as attempting to plead merely a claim for corporate waste and mismanagement

Defendants' first ground for dismissal contended that the complaint allegedly pleaded only a cause of action for corporate waste or mismanagement. For this proposition defendants cited the Panel decision in Schoenbaum v. Firstbrook, 405 F.2d 200 (2d Cir. 1968); O'Neill v. Maytag, 339 F.2d 764, 768 (2d Cir. 1964); and Birnbaum v. Newport Steel Corp., 193 F.2d 461, 464 (2d Cir. 1952). Citation of these particular authorities for such a proposition is incomprehensible and is little short of intellectual dishonesty since, although the cited cases did hold what defendants ascribe to them, they have either been reversed or overruled on the very points for which they were cited below.

Thus, although defendants noted that Schoenbaum, had been "modified on other grounds," the fact is that it was reversed en banc on the precise ground that the directors there had breached their fiduciary duties, and the breach operated as a fraud and

deceit upon the stockholders and violated Rule 10b-5 since it touched upon the purchase and sale of securities. Schoenbaum v. Firstbrook, 405 F.2d 215, 219-20 (2d Cir. 1968, en banc).

Similarly, defendants' citation of O'Neill v. Maytag, supra, and Birnbaum, simply ignores the Supreme Court's decision in Superintendent of Insurance v. Bankers Life & Cas. Co., supra, 404 U.S. 6 (1971), and A. T. Brod & Co. v. Perlow, supra, 375 F.2d 393, 397 (2d Cir. 1967); and the later decision of this Court in Schlick v. Penn-Dixie Cement Corp., 507 F.2d 374, 379-80 (2d Cir. 1974), which defendants cited but evidently did not read. This Court there held:

"It is well to put to rest . . . a slow-to-die contention advanced by appellees principally in oral argument but to some extent in their brief---a contention first authoritatively set forth in Birnbaum v. Newport Steel Corp., 139 F.2d 461 (2d Cir.), cert.denied, 343 U.S. 956, . . . (1952), viz., that § 10(b) 'was directed solely at that type of misrepresentation or fraudulent practice usually associated with the sale or purchase of securities rather than at fraudulent mismanagement of corporate affairs. . . . Here, appellees tell us, all that appellant is complaining about is 'corporate mismanagement,' and as such is in the wrong forum. As long ago as A. T. Brod & Co. v. Perlow, 375 F.2d 393, 397 (2d Cir. 1967), this Birnbaum proposition was no longer the law of this circuit as 10b-5 was there construed to include 'all fraudulent schemes in connection with the purchase or sale of securities, whether * * * a garden type variety of fraud, or * * * a unique form of deception.' While Birnbaum was principally relied upon in O'Neill v. Maytag, supra, which in turn was relied upon by the court below in terms of stating the restrictive view, the authority of these cases (Birnbaum and O'Neill) was . . . 'seriously undercut' by Schoenbaum v. Firstbrook, 405 F.2d 215 (2d Cir. 1968), rev'g, 405 F.2d 200, cert.denied 395 U.S. 906, . . . (1969). Thus Judge Feinberg could write in Popkin v. Bishop, 464 F.2d 714, 718 (2d Cir. 1972), that 'assertions by a defendant that the misconduct complained of "really" amounts to "just" corporate

mismanagement will not cut off a plaintiff's federal remedy. Where Rule 10b-5 properly extends, it will be applied regardless of any cause of action that may exist under state law.' In any event, any lingering doubts as to the vitality of this Birnbaum proposition were firmly interred by the Supreme Court in Superintendent of Insurance v. Bankers Life and Casualty Co., 404 U.S. 6, 10-11 n. 7, . . . (1971), where the Court stated that it is not 'sound to dismiss a complaint merely because the alleged scheme does not involve the type of fraud that is "usually associated with the sale or purchase of securities"' . . . It can thus truthfully be said . . . that '[a]fter Supt. of Insurance, then, Birnbaum survives significantly only for the buyer-seller requirement. . ."

In the Court below defendant argued that Schlick has to some extent been superseded by Blue Chip Stamps---a contention with which plaintiffs obviously disagree since Blue Chip addresses itself to the question of the plaintiff's standing and not to the nature of the alleged fraud or the identity of the defendant, which remains governed by Superintendent of Insurance, supra---and suggested that the Court should follow the Tenth Circuit's decision in Rochelle v. Marine Midland Grace Trust Co., ___ F.2d ___, CCH Sec.L.Rep. ¶ 95,562, at pp. 99,802-03 (10th Cir. 1976), which defendants contended required the dismissal of the present complaint. However, Rochelle does not require that result, and to the extent it may be deemed to differ from the tests laid down in Schlick, obviously in this Circuit Schlick controls.

Rochelle was a suit brought by a Chapter X Trustee against the former directors of his company, charging them with various misrepresentations and omissions of material fact in connection with the purchase or sale of securities, plaintiff purporting to sue both on behalf of the corporation and its

stockholders and/or creditors. As to the stockholders and creditors, the Tenth Circuit held that the Trustee lacked standing to sue. The Trustee's problem in suing for the corporation was that although it was both a purchaser and seller of its own securities (and so had standing), the corporation itself was able to show no injury resulting from the alleged violations of Rule 10b-5: Its purchases of its own securities had been made either at their face value or below (so that there could be no damage on account of them), and its resale of a repurchased debenture at below the purchase price was not causally connected to the alleged misrepresentations or omissions. Thus the Tenth Circuit said, loc.cit.:

"Rochelle's theory is thus corporate mismanagement, which he has tried to fit within the roomy language of Superintendent of Life Insurance [sic] v. Bankers Life and Casualty Co. ["Bankers Life"] (1971) 404 U.S. 6. Although Section 10(b) was not meant to cover 'internal corporate mismanagement,' '[t]he crux of the present case is that Manhattan suffered an injury as a result of deceptive practices touching its sale of securities as an investor.' (Id. at 12-13). Bankers Life was undoubtedly intended to prevent courts from reading the phrase 'in connection with' grudgingly. The Court did not try to describe how close to the securities transaction the mismanagement must be before it is deemed to touch the transaction. No comprehensive definition of these tactile concepts is practicable; rather[,] each alleged scheme must be examined in its own context to determine whether the deception or mismanagement caused injury to persons suing who bought or sold securities and whether their wrongful conduct sullied the 'purity of the security transaction and the purity of the trading process.' (404 U.S. at 9-10). (See Smallwood v. Pearl Brewing Co. (5th Cir. 1974) 489 F.2d 579, 592, 594-95.) We assume, arguendo, that the alleged mismanagement did taint the purity of the marketing of these debentures and that investors who purchased them thereby suffered injury. Rochelle cannot sue for them because Caplin v. Marine Midland Grace Trust Co., supra, [406 U.S. 416 (1972),] disables him from doing so.

"Nor can Rochelle maintain this action on Sunset's behalf. In this case, the 'in connection with' requirement bleeds into the requirement that the plaintiff suffer some damages. Sunset could not successfully sue because it lost nothing in its capacity as an investor on the issuance of its debentures. It received full value for the securities; that the directors later frittered away the funds on losing real estate ventures does not mean that Sunset suffered a loss compensable under the federal securities laws. The nexus between the securities transaction and the alleged losses due to mismanagement is too attenuated in this case to use as a predicate for Section 10(b) liability. We thus conclude that the district court correctly dismissed Rochelle's Section 10(b) and Rule 10b-5 claims against all of the defendants."

It is clear that Rochelle is neither contrary to Schlick nor required the dismissal of the complaint below. It might have required such a dismissal only if the complaint herein had been limited to Counts I and III, with plaintiffs making the post hoc ergo propter hoc contention that defendants' actual post-offering self-dealing and thefts (the wrongdoing alleged in Count III) proved that there had been non-disclosures of an intention to despoil the corporate plaintiffs at the time of the initial offering (Count I). In such a case it could arguably be said, in the words of the Tenth Circuit, that the fact

"that the [defendants] later frittered away the funds on losing . . . ventures does not mean that [plaintiffs] suffered a loss compensable under the federal securities fraud laws. The nexus between the securities transaction and the alleged losses due to mismanagement is too attenuated . . ."

But that argument cannot properly be made here. In the first place, Count I itself alleges misrepresentations or omis-

sions having nothing to do with the subsequent waste and mismanagement, or outright looting, of the corporate plaintiffs---specifically the misrepresentation concerning the need for a voting trust agreement and the fraudulent allocation to Barnett of the full value of La Bazoche (and Walborg), by which he became a majority stockholder of Rockley for no capital investment of his own. In this respect Barnett's scheme resembles nothing so much as the fraudulent scheme condemned in Superintendent of Insurance itself.

Secondly, Rochelle obviously is inapplicable once attention is focused upon Counts II and IV of the complaint in suit, each of which complains of the non-disclosure of the prior spoliation of Rockley and its subsidiary corporations, in connection with subsequent purchases of Rockley's securities by the individual plaintiffs. These omissions certainly involve facts which would have been deemed material by the individual plaintiffs, who might have decided to allow their prior investment go down the drain rather than to sink an additional half million dollars or more into an enterprise which might no longer be susceptible of salvage, and giving general releases to the malefactor in the bargain. Certainly full disclosure of the true facts in December 1975 would have precluded the possibility that plaintiffs Baretge, Trimble and Rockley Associates, S.A. would have made the additional stock purchases alleged in Count II while Barnett remained in control. Such disclosures might have led to his ouster in December 1975, rather than in March 1976, and would thereby have saved the

individual and corporate plaintiffs the further substantial losses which occurred during Barnett's final mop-up operations prior to departing under cover of general releases.

Thus defendants' citation of Rochelle to the Court below turned upon a few words of an opinion taken out of context and completely ignored the facts alleged in the complaint. The complaint is not deficient as pleading "merely" a claim for corporate waste and mismanagement. Fairly read, it alleges a series of stock transactions the primary if not sole object of which was to vest the culprit with control of a group of corporations so that he could loot them, and, when the looting was complete or virtually so, to get out by means of a further sale of securities, with the apparent (but illusory) protection of general releases.

- (b) Each of the individual plaintiffs is a conventional purchaser of securities and has standing to sue under Rule 10b-5

As an examination of the complaint demonstrates, allegations are sufficiently made that all of the individual plaintiffs (Baretge, Macheras, Trimble and Rockley Associates, S.A.) were purchasers of securities in the transactions complained of in Counts I and IV, and all but Macheras were purchasers of securities in the transactions complained of in Count II, in each case "purchasers" in the conventional sense. Moreover, as respects the purchases in March 1976 which are complained of in Count IV, the individual plaintiffs were purchasers of securities from Barnett himself.

- (c) Each of the corporate plaintiffs has standing to sue for violation of Rule 10b-5 because it contributed part of the consideration for the purchase of Barnett's stock

Count IV of the complaint is brought by all of the plaintiffs against all of the defendants, including Julienne and Messerli. It is respectfully submitted that each of the plaintiffs, including the corporate plaintiffs which purchased no securities, qualify as Rule 10b-5 plaintiffs at least as to some of the relief sought by Count IV, because each of them gave up, and was required to give up, valuable considerations in connection with the purchase of Barnett's stock by the individual plaintiffs, at least to defendants Barnett and Julienne.

In the first place, each of the plaintiffs was compelled to give general releases to Barnett and his wife, and those releases were evidently (and understandably) required by Barnett, without disclosure by him of what wrongdoing was likely thereafter to be uncovered (and liability thereon presumably extinguished), and in the face of the imminent bankruptcy of the corporate enterprise. Part of the relief sought under Count IV is a declaration of the invalidity of the general releases since they were procured by means of violations of Rule 10b-5, and were unquestionably given "in connection with the purchase or sale of any security," and, realistically, were the major consideration in that stock purchase transaction, albeit an illusory one.

If, as alleged in Count IV, the purchase and sale of Barnett's stock violated Rule 10b-5, the releases given to him

and his wife as a major part of the consideration for his sale of his stock may be avoided by virtue of section 29(a) of the Exchange Act, 15 U.S.C. § 78cc(a), on the strength of Barnett's material omissions and misrepresentations, backed by the financial pressure imposed on the plaintiffs by the threatened foreclosure by creditors of one or more of the corporations.

In Pearlstein v. Scudder & German, 429 F.2d 1136, 1143 (2d Cir. 1970), this Court said:

"Section 29(a) of the Securities Exchange Act holds void any stipulation obligating a party to waive compliance with the Act. Although the lower court held that waivers of rights under the Act may be given effect if the waivers occur after the commencement of suit, the cases cited only stand for the proposition that the remedial right of access to the courts after an active controversy has arisen can be waived knowingly in favor of arbitration. Here it is difficult to say that Pearlstein's waiver was knowing, given the apparent lack of any inducement to give up his rights other than financial pressure. But if the waiver were knowing, it would not secure some desirable end such as arbitration, easily compatible with the broad purpose of the Act, but would instead serve only to legalize the very extension of credit which the margin requirements seek to prevent and which suits such as this one serve to discipline. Indeed, brokers could routinely extend credit beyond margin simply by delivering bonds to third-party lenders before they were paid for by the customer, and then immediately commencing suit against the customer for the difference, obtaining a waiver in return for a stay of judgment. Such a possibility clearly militates against any bending of the language of Section 29(a) to accommodate the stipulations here involved." (Emphasis added).

The analogy here is plain. If the principal of a corporation is permitted to loot the corporation, and in the face of creditors' threats of foreclosure, to sell his stock to those who had contributed its entire equity, without disclosing to them material

facts relating to the parlous condition of the corporation or the value of what they are being forced to purchase, and as part of the purchase price obtaining from them and from the corporations involved general releases of any and all wrongdoing---and such releases are upheld either because the corporate victims themselves neither purchased nor sold a security (and, as defendants argued in the Court below, much of the relief sought must necessarily be brought by them in their corporate capacity)---Rule 10b-5 will prove an illusory protection against the very wrongdoing which it seeks to prevent "and which suits such as this one serve to discipline."

In addition to the general releases which Barnett extorted for himself and his wife from each of the plaintiffs, the purchase price for Barnett's stock included a commitment by Walborg to pay to Barnett a total of \$60,000 in nine monthly instalments, and he acquired from La Bazoche a valuable Mercedes Benz automobile. Walborg has not paid any portion of the \$60,000, and part of the relief sought in the present action is a declaration that its promise to pay that amount was procured by fraud and is unenforceable.*

Thus, while not "purchasers" in the conventional sense, each of the corporate plaintiffs gave consideration for the purchase of a security, and should have standing to complain of a violation of Rule 10b-5 in connection with such purchase, cf., Eason v. General Motors Acceptance Corp., 490 F.2d 654, 659-60

*The Mercedes Benz has apparently been sold and leased back, so that it can no longer be recovered from Barnett.

(7th Cir. 1973)(alternative holding), in which Judge (now Justice) John Paul Stevens said:

"The plaintiffs in this case were certainly 'investors' in the transaction which is allegedly tainted by fraud. Their interest as stockholders of Bank Service Corporation was apparently sufficient to induce them to execute substantial personal guarantees. As individual guarantors they were direct parties to the transaction in dispute. If, as plaintiffs have alleged, the transaction was consummated in violation of Rule 10b-5, we believe the plaintiffs, as investors and as principals in the transaction, suffered a legal injury which may be redressed by a federal court."

Here the corporate plaintiffs gave up general releases rather than guarantees, but in context that is a distinction without a difference. The seller of the stock (Barnett) was apparently as insistent on receiving those releases as GMAC had been on receiving the individual guarantees in Eason, and the parties giving them were as much "direct parties to the transaction in dispute" as were the guarantors in Eason.

Moreover, whereas the guarantors in Eason became liable under their guarantees only upon the happening of a contingency---the non-payment of the primary obligations, the corporate plaintiffs here, by hypothesis, unconditionally and immediately gave up something of value---their extensive damage claims against both Barnetts for breach of fiduciary duty and misappropriation of corporate property and assets. On authority of Eason v. GMAC, supra, the corporate plaintiffs themselves have standing to maintain an action against both Barnetts to set aside releases procured in violation of Rule 10b-5, since the consideration they gave was given to both Barnetts, and complete relief cannot be had without joining Julianne as a defendant to Count IV.

- (d) Defendant Julianne Barnett
is a proper defendant to the
Rule 10b-5 claim in Count IV
although she sold no securities

As we have observed, defendant Julianne was a named beneficiary of the releases, and actively participated in the embezzlement of the "key man" life insurance policy, which Barnett transferred to her immediately after stealing it, over which which she exercised dominion by making herself the beneficiary. These events immediately followed the sale of securities complained of in Count II, and immediately preceded the sales of securities by Barnett complained of in Count IV---and suggests conspiracy.

In very similar circumstances, the First Circuit held that it would be inappropriate to decide facts so suspicious on a motion for summary judgment, Ferguson v. Omnimedia, Inc., 469 F.2d 194, 197-98 (1st Cir. 1972), and we would think that conclusion would be a fortiori true on a naked motion to dismiss. In Ferguson, as here, the primary wrongdoer's wife was charged with participation in the husband's primary wrongdoing. Like Julianne, the wife there, Lisabeth, was a director of the corporation, although unlike Lisabeth there, Julianne here was not an officer. Following a review of her various corporate roles and alleged knowledge of accountancy (since that was in issue there), the First Circuit said:

"Additionally, Lisabeth's alleged participation in the preparation and filing of articles of amendment containing a false statement, and her alleged acquiescence, as an officer and director, in the issuance of stock to Gibson and her husband without lawful consideration, may possibly be shown to have been overt acts in furtherance of such a conspiracy, whether or not the

appellant actually relied upon either or both acts. If Lisabeth took part in a conspiracy, she may be held responsible for the acts of a co-conspirator that actually misled the appellant into buying stock (such as her husband's furnishing of a false balance sheet), even if she herself did not participate in those acts. . . .

"In a conspiracy case, agreement is rarely out in the open, and proof of conscious complicity may depend upon the careful marshalling of circumstantial evidence and the opportunity to cross-examine hostile witnesses. . . . As in the present case, summary judgment procedures are often not a sufficient substitute for trial."

Given the fact that in Messerli's state court action Barnett himself has submitted affidavits purporting to attest to the approval of Walborg's board of directors to the purported transfer of ownership of the insurance policy to himself, and it being conceded that the Walborg board consisted of three individuals, of whom two were Barnett and Juliette, Juliette cannot be heard to attempt to pass herself off as an innocent recipient of corporate property from her husband with no knowledge, or the basis for knowledge, of the impropriety of the manner in which he had acquired it. She either herself participated in the purported approval of the transfer of the policy, or failed to inquire into how her cestui que trust had been caused to give up ownership of a valuable asset without her prior knowledge or approval.

- (e) Defendant Messerli is a proper defendant to the Rule 10b-5 claim in Count IV although she sold no securities

While much of the rationale of Ferguson would also apply to Messerli---who was a de facto officer of Walborg and actually executed the documents purporting to transfer the insur-

ance policy on Barnett's life, presumably without asking to see the non-existent directors' resolution or stockholder consent, a transfer which occurred so shortly after Barnett's purported forgiveness of her loan of \$20,000, and right after a purported increase of her salary from \$14,000 to \$26,000 per year---still the situation of defendant Messerli stands on a somewhat different footing because the general releases extorted in the transaction complained of in Count IV do not run to her. Moreover, the urgency of joining her in Count III of the present action is not as great because she and the present corporate plaintiffs are presently involved in litigation in the state court which raises some of the same issues.*

However, although the releases given by all plaintiffs in terms run only to Barnett and Julianne, and not to Messerli, in her state court papers Messerli brazenly sought to immunize her own wrongful acts by attempting to include herself in the assumed protection of the general releases given to Barnett and Julianne, stating in a letter which is now part of the state court record, that:

"I have consulted with an attorney who has advised me that Norman Barnett's action in cancelling the outstanding loan was well within his real and apparent authority as chief executive officer. It is also my understanding

*While no decision by this Court respecting Messerli would normally be appropriate since she was not served below and thus is not a party, Judge Brieant did dismiss the complaint against her, and a reversal of his ratio decidendi would presumably reinstate it against her as well. She has appeared in the state court by the same attorneys who represent the Barnetts here, so that she is not without defenders.

that you have delivered to Norman Barnett a general release for any and all of his actions which release would clearly include the cancelling of the promissory note."

Moreover, Messerli's Reply to the corporate plaintiffs' counterclaims contains the following two defenses:

"First Affirmative Defense As to All Counterclaims: On or about May 3, 1976, prior to the commencement of this action, [sic; after the commencement of Messerli's action but two days prior to the assertion of their counterclaims], the defendants Rockley Group, Walborg and Coblentz Bag commenced an action in the United States District Court for the Southern District of New York against plaintiff for the same causes of action as are alleged in the answer herein.

"Third Affirmative Defense with Respect to Counterclaims: If there was any wrongdoing in connection with the loans made to plaintiff or their cancellation or the alleged transfer of an insurance policy by Barnett, such wrongdoing was on the part of Norman N. Barnett and prior to this action, defendants released him from all liability with respect to such wrongdoings and said release is a bar to the counterclaims in this action."

These allegations suggest that in the event of a reversal and remand here and after service of process upon Messerli, the Barnetts' motion will be renewed by Messerli, who might regard herself as not being bound by anything that transpired here because she was not actually before this Court. However, the District Court is entitled to guidance as to the scope of this Court's decision, particularly given the District Court's grudging approach to the remedies afforded by Rule 10b-5, cf., GAF Corp. v. Milstein, 453 F.2d 709, 722 nt. 27 (2d Cir. 1972). Messerli's conduct in the state court demonstrates that she intends to use the pendency of this action and the fact of the fraudulently obtained releases to cloud the rather simple issues

between her and the corporate plaintiffs in that action, which fact warrants her being included as a party in the present action insofar as constitutional limitations permit, which, we submit, they do.

Moreover, apart from the obvious interrelationship between Messerli and the Barnetts and her effort to bring herself within the releases which are so large a part of the relief sought herein, Messerli has received some of the more tangible fruits of Barnett's violations of Rule 10b-5, in that the forgiveness of her \$20,000 indebtedness to Rockley and/or Walborg followed immediately upon the investment complained of in Count II, and was accompanied by a near-doubling of her salary, both of which were in turn followed almost immediately by her aiding and abetting Barnett's embezzlement of the "key man" life insurance policy on his own life, a quid pro quo which is the connecting link between two related violations of Rule 10b-5. Plaintiffs respectfully submit that the acts of Messerli are sufficiently integral to Barnett's securities frauds as to make her a culpable participant in those frauds and a proper defendant under Counts IV and III.

- (f) Even if Julianne and Messerli are not held to be properly joined as defendants to Count IV, the allegations of Count III are so intimately related to the securities frauds that "pendent jurisdiction of the person" makes joinder proper

From what has already been said it should be apparent that proof of the allegations of Count IV is essentially coexten-

sive of the proof that will be required for the allegations of Count III, which would make that Count properly pendent to a well-pleaded claim under the jurisdiction-conferring Exchange Act, both as to Barnett and also as to Julienne. To require plaintiffs to pursue Julienne in a separate state court action for corporate waste and breach of fiduciary duty (which might properly have to await the determination of the action below because of the releases given to her) can scarcely be productive of the conservation of judicial time and energies.

Even if the Court were to disagree with our contention that the acts of Julienne and Messerli are sufficiently close to the securities violations of Barnett as to warrant their being made parties to Count IV, they are sufficiently closely related to warrant their joinder, if only with respect to the allegations of Count III, on the basis of the doctrine of "pendent jurisdiction" of the person," which this Court has recognized in areas other than the Exchange Act, Astor-Honor, Inc. v. Grosset & Dunlap, Inc., 441 F.2d 627, 629 nt. 2 (2d Cir. 1971); cf., Schwartz v. Eaton, 264 F.2d 195 (2d Cir. 1959, dictum), and which other courts have recognized in Exchange Act suits, see, e.g., In re Penn Central Securities Litigation, 338 F.Supp. 436, 438 (E.D.Pa. 1972); Emerson v. Falcon Mfg., Inc., CCH Sec.L.Rep. ¶ 93,247, pp. 91,516-17 (S.D.Texas 1971); Puma v. Marriott, 249 F.Supp. 1116, 1121 (D.Del. 1969); Sprayregan v. Livingston Oil Co., 295 F.Supp. 1376, 1379 (S.D.N.Y. 1968); Lyons v. Marrud, Inc., 46 FRD 451, 455-56 (S.D.N.Y. 1968); Kane v. Central American Min. &

Oil, Inc., 235 F.Supp. 559, 565-67 (S.D.N.Y. 1964); Cooper v. North Jersey Trust Co., 226 F.Supp. 972, 980-82 (S.D.N.Y. 1964); Townsend Corp v. Davidson, 222 F.Supp. 1, 4 (D.N.J. 1963); Collins v. Bush Mfg. Co., 19 FRD 297, 298-99 (S.D.N.Y. 1956; dictum); Miller v. Hano, 8 FRD 67, 71-72 (E.D.Pa. 1947).

There are, of course, numerous well-reasoned decisions rejecting the doctrine of pendent jurisdiction of the person--- particularly where the "pendent" defendant is not subject to suit in the district---including especially Trussell v. United Underwriters, Ltd., 236 F.Supp. 801, 803-05 (D.Colo. 1964); Wilensky v. Standard Beryllium Corp., 228 F.Supp. 703, 705-06 (D.Mass. 1964); ILGWU v. Shields & Co., 209 F.Supp. 145, 147-49 (S.D.N.Y. 1962); Phillips v. Murchison, 194 F.Supp. 620, 622 (S.D.N.Y. 1961), and in most situations we would favor the rule denying pendent jurisdiction of a party not properly joined in a federal jurisdiction-conferring claim.

However, the facts of the present case are such that even if this Court were to conclude that neither Messerli nor Julianne directly participated in Barnett's violations of the Exchange Act, their wrongdoing is so inextricably tied to his securities frauds as to warrant exposing them to suit in the same action. On this point, this Court said in Astor-Honor, supra, 441 F.2d at 629-30 (discussing the limitations and meaning of UMW v. Gibbs, supra):

"Although the pendent claim in Gibbs did not include a party not named in the federal claim, Mr. Justice Brennan's language and the common sense considerations underlying it seem broad enough to cover that problem

also. . . . A plaintiff with claims against three alleged conspirators for the same set of acts 'would ordinarily be expected to try them all in one judicial proceeding,' assuming that all defendants were subject to the process of the court. It would be an unjustifiable waste of judicial and professional time---indeed a travesty on sound judicial administration---to allow Astor to try its unfair competition claim against Buckley and Bantam in federal court but to require it to prosecute a claim involving precisely the same facts against Grosset 'in a State court a block away. The absence of any constitutional barrier to entertaining a sufficiently related state claim against a person who was not party to the federal claim was recognized, prior to Gibbs, in cases involving compulsory counter-claims under F.R.Civ.P. 13(a)," (Emphasis added).

On authority of Astor-Honor, supra, there plainly is no constitutional impediment to subjecting defendants Julianne Barnett and Messerli---both of whom reside in New York City---to suit under Count III, even if they are not properly joined in Count IV, since Count III is so intimately and inextricably related to the overall fraudulent scheme which manifestly involved the sale and purchase of securities.

Conclusion

Thus the decision below, dismissing the complaint for failure to state a claim under Rule 10b-5, and consequently for lack of jurisdiction of the subject matter and of the pendent claims asserted in Count III, is not sustainable on the basis actually urged upon the Court below by the defendants, or on any corollaries derived from their arguments. The Court below had jurisdiction of the securities fraud claims, and it has jurisdiction of all three defendants either because each of them participated in the securities fraud sufficiently to be made answerable therefor, or because of pendent jurisdiction.

POINT III

THE COMPLAINT SATISFIES THE PARTICULARITY REQUIREMENTS OF RULE 9(b) OF THE FEDERAL RULES OF CIVIL PROCEDURE

An alternative basis for dismissing the complaint urged by defendants on the Court below was that the complaint failed to satisfy the particularity requirements of Rule 9(b) of the Federal Rules of Civil Procedure, citing Shemtob v. Shearson, Hammill & Co., 448 F.2d 442 (2d Cir. 1971); and Segal v. Gordon, 467 F.2d 602 (2d Cir. 1971). However, in Shemtob, the effort was to create a Rule 10b-5 claim out of an alleged violation of a Stock Exchange Rule, whereas in Segal summary judgment was granted to two directors who adduced evidence, conformably to Rule 56(e), that they were not responsible for the alleged wrongdoing, and plaintiff failed to rebut that evidentiary showing.

These cases have no practical application to the complaint in suit here. If anything, the complaint errs on the side of overparticularization, to the point of pleading evidentiary facts, and its sufficiency is sustained under Rule 9(b) of the Federal Rules by Schlick v. Penn-Dixie Cement Corp., supra, 507 F.2d 374, 378-79 (2d Cir. 1974):

"We go first to the 10b-5 count of the complaint. That count does allege generally 'the engagement in a course of business which operated as a fraud and deceit on the purchasers and holders of Continental stock.' If that were all that were alleged, it would fall within this court's rule that 'mere conclusory allegations to the effect that defendant's conduct was fraudulent or in violation of Rule 10b-5 are insufficient.' Segal v. Gordon, 467 F.2d at 607, quoting Shemtob v. Shearson, Hammill & Co., 448 F.2d 442, 444 (2d Cir. 1971), and

O'Neill v. Maytag, supra. But here the complaint contains more than conclusory allegations. Paragraph 15 specifically alleges that Continental bank accounts were utilized by Penn-Dixie as compensating balances for Penn-Dixie's own borrowings and for Penn-Dixie's benefit without compensation or benefit to Continental, thereby depriving Continental of its ability to use its own capital to expand its business and thereby obtaining a more favorable merger exchange ratio. . . . While all of these allegations are stated on information and belief, and there are cases holding that allegations of fraud based on information and belief usually do not satisfy the degree of particularity required by Fed.R. Civ.P. 9(b), . . . the particularity requirement may be satisfied if, as here, the allegations are accompanied by a statement of the facts upon which the belief is founded. . . . In any event, Rule 9 must be construed in conjunction with Rule 8, . . . and a complainant is not required to plead evidence. . . . We consider Rule 9 sufficiently complied with here."

Without further belaboring the facts and the allegations of the complaint, which we have discussed in prior portions of this Brief, plaintiffs respectfully submit that the complaint in suit amply satisfies the test enunciated in Schlick, and that defendants' motion seeking dismissal of the complaint under Rule 9(b) of the Federal Rules is wholly lacking in merit and will not support the dismissal of the complaint by the Court below.

CONCLUSION

THE COURT BELOW ERRED IN IMPOSING THE REQUIREMENT THAT A RULE 10b-5 DEFENDANT BE THE PRIOR OWNER OF THE SECURITIES SOLD TO PLAINTIFF, AND IMPROPERLY DISMISSED THE COMPLAINT. THE COMPLAINT IS NOT DEFICIENT AS PLEADING "MERELY" CORPORATE WASTE AND MISMANAGEMENT, NOR IS IT INSUFFICIENTLY PARTICULARIZED TO COMPLY WITH RULE 9(b) OF THE FEDERAL RULES OF CIVIL PROCEDURE. IT SUFFICIENTLY STATES A CLAIM AGAINST ALL THREE DEFENDANTS, AND THE DISMISSAL BELOW SHOULD BE REVERSED WITH INSTRUCTIONS.

Respectfully submitted,

CARRO, SPANBOCK, LONDIN, RODMAN & FASS
Attorneys for Plaintiffs-Appellants
1345 Avenue of the Americas
New York, New York 10019
Tel. (212) PLaza 7-2400

REGINALD LEO DUFF,
Of Counsel.

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PLAINTIFFS

DEFENDANTS

BRIEANT, J.C.

BARETGE, MAXIME C.
 ROCKLEY ASSOCIATES, SA
 MACHERAS, PIERRE
 TRIMBLE, DAVID W.
 THE ROCKLEY GROUP, INC.,
 LA BAZOCHE, INC.,
 WALBORG CORPORATION, and
 COBLENTZ BAG CO., INC.,

BARNETT, NORMAN N.
 BARNETT, JULIENNE
 MESSERLI, VI L.

J.G.

CAUSE

Common law fraud in sale of securities
 and corporate looting.

ATTORNEYS

CARRO, SPANBOCK, LONDIN, RODMAN & FASS
 10 East 40th St.
 New York, N.Y. 10016
 889-3600

☐ CHECK
 HERE
 IF CASE WAS
 FILED IN
 FORMA
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FILING FEES PAID

DATE	RECEIPT NUMBER	C.D. NUMBER
MAY 3 1976	69758	
MAY 11 1976	70439	

STATISTICAL CARDS

CARD	DATE MAILED
JS-5	
JS-6	

76 Civ. 1994 Maxime C. Baretge ET. AL. vs. NORMAN N. Barnett, LI. AL.

DATE	NR.	PAGE, 2	PROCEEDINGS
05-03-76	(1)	Filed complaint. Issued summons.	
5-24-76		Fld Stip & Order that defts N. N. Barnett and J. Barnett's time to answer the complt is ext to 6-14-76....Bricant, J.	
6-23-76		Fld Defts Barnetts's notice of motion to dismiss complt pur to Rule 9 and 1ret 6-2-76-.OAM Rm 501.	
6-23-76		Fld Defts' Memo of law in support of their(Barnetts) motion to dismiss.	
6-29-76		Fld Pltffs' memo in opp ition to defts' motion to dismiss complt.	
7-2-76		Fld Stip & Order that defts Barrent and Barnett motion to dismiss is adj to 7-8-...Bricant, J.	
7-8-76		Fld Reply memo of defts Barnett, Morman & Barnett, Julianne in support of motio to dismiss.	
7-9-76		Fld Memo End on bk of motion fld 6-23-76—Motion granted. Complt dismissed as all defts, including Messerli. So Ordered.....Bricant, J. m	
7-14-76		Fld Judgment....Order that deft N. N. Barnett, J. Barnett and VI L. Messerli, have judgment vs pltffs M. C. Baretge, Rockley Assos, S.A. Pierre Marcheras, D.W. Trimble, the Rockley Group, Inc., La Dacoste, Inc., Walborg Corp and Cobb Bag Co., Inc., dismissing complt.....R.P. Burghardt, Clerk ent 7-15-76.	
3-12-76		Fld Pltffs' Notice of Appeal to USCA from judg mt 7-14-76...Copies mailed on 8-16-76 To: Baton, Van Nibbeling & Greenbaum	

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(Notice of Appeal)

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

-----X
MAXIME C. BARETGE, ROCKLEY ASSOCI- :
ATES, S.A., PIERRE MACHERAS, :
DAVID W. TRIMBLE, THE ROCKLEY GROUP, :
INC., LA BAZOCHE, INC., WALBORG :
CORPORATION and COBLENTZ BAG CO., INC., :

Plaintiffs, :

-against- : 76 Civ. 1994 (CLB)

NORMAN N. BARNETT, JULIENNE : NOTICE OF APPEAL
BARNETT and VI L. MESSERLI, :

Defendants. :
-----X

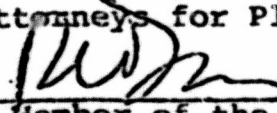
S I R S :

PLEASE TAKE NOTICE, that the plaintiffs MAXIME C. BARETGE, ROCKLEY ASSOCIATES, S.A., PIERRE MACHERAS, DAVID W. TRIMBLE, THE ROCKLEY GROUP, INC., LA BAZOCHE, INC., WALBORG CORPORATION and COBLENTZ BAG CO., INC., hereby appeal to the United States Court of Appeals for the Second Circuit from a Judgment entered herein on the 14th day of July, 1976 upon a Memorandum Endorsement dated July 9, 1976, Hon. CHARLES L. BRIEANT, U.S.D.J., which dismissed the Complaint herein for failure to state a claim for relief under Rule 10b-5 under the Securities Exchange Act of 1934, and for lack of jurisdiction of the subject matter, and from each and every part of said Judgment.

Dated: New York, New York
August 12, 1976

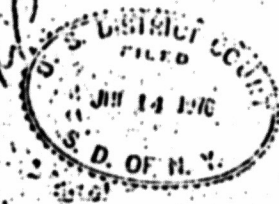
Yours, etc.,

CARRO, SPANBOCK, LONDIN, RODMAN & FASS
Attorneys for Plaintiffs

By  :
A Member of the Firm
10 East 40th Street
New York, New York 10016
Tel. (212) 889-3600
App. 1

Judgment, Appealed From

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UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

----- X
MAXIME C. BARETGE, ROCKLEY
ASSOCIATES, S.A., PIERRE MARCHERAS,
DAVID W. TRIMBLE, the ROCKLEY GROUP,
INC.; LA BAZOCHE, INC., WALBORG
CORPORATION and COBLENTZ BAG CO., INC.

76 Civil 1994 (CLB)

JUDGMENT

Plaintiffs

-against-

NORMAN N. BARNETT, JULIENNE
BARNETT and VI L. MESSERLI

Defendants
----- X

Defendants Barnett having moved the Court for an order dismissing the complaint pursuant to Rules 9 and 12, of the Federal Rules of Civil Procedure, and the said motion having come on to be heard before the Honorable Charles L. Bricant, United States District Judge, and the Court thereafter on July 9, 1976, having handed down its memorandum endorsement granting the said motion as to all defendants including defendant Messerli, it is,

ORDERED, ADJUDGED and DECREED: That defendants NORMAN N. BARNETT, JULIENNE BARNETT and VI L. MESSERLI, have judgment against plaintiffs MAXIME C. BARETGE, ROCKLEY ASSOCIATES, S.A., PIERRE MARCHERAS, DAVID W. TRIMBLE, the ROCKLEY GROUP, INC., LA BAZOCHE, INC., WALBORG CORPORATION and COBLENTZ BAG CO., INC., dismissing the complaint.

Dated: New York, N.Y.
July 14, 1976

Raymond F. Beuglandt
Clerk

Memorandum Endorsement

Endorsement

MAXIME C. BARETGE; ROCKLEY ASSOCIATES, S.A.; PIERRE MACHERAS; DAVID W. TRIMBLE; THE ROCKLEY GROUP, INC.; LABAZOCHE, INC.; WALBORG CORPORATION; and COBLENTZ BAG CO., INC., Plaintiffs v. NORMAN N. BARNETT; JULIENNE BARNETT and VI L. MESSERLI, Defendants. 76 Civ. 1994-CL

A careful reading of this complaint shows with respect to Counts I and II that neither the moving defendants nor Messerli were "sellers" of securities in violation of Rule 10b-5; nor were plaintiffs buyers thereof from defendants. However, the pleading be characterized or described, it fails to state a claim under §10b of the 1934 Act in either of these counts. Blue Chip Stamps v. Manor Drugstores, 421 U.S. 723 (1975). Even before Blue Chip we had been cautioned more than once against "a trend we have observed with disturbing frequency, namely, invocation of the salutary anti-fraud provisions of the federal securities laws in cases where those provisions are wholly inappropriate and wide of the Congressional mark." [Quoted from Kavit v. A. L. Stamm & Co., 491 F.2d 1176 (2d Cir. 1974), relying in turn on Ryan v. J. Walter Thompson Co., 453 F.2d 444, 445 (2d Cir. 1971)].

Under the circumstances, there is no basis to exercise pendent jurisdiction.

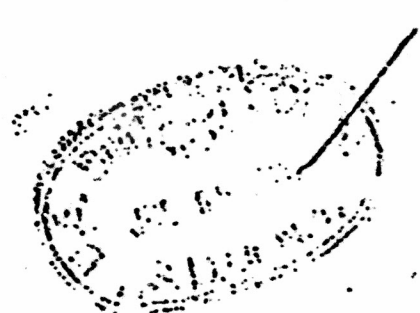
Motion granted. Complaint dismissed as to all defendants, including Messerli.

So Ordered.

Dated: New York, New York
July 8, 1976

Charles L. Briant

CHARLES L. BRIANT
U. S. D. J.



JUL 09 1976

Notice of Motion

United States District Court
Southern District of New York

-----X
Maxime C. Baretge, Rockley
Associates, S.A., Pierre Macheras;
David W. Trimble; the Rockley Group,
Inc.; La Bazoche, Inc.; Walborg
Corporation; and Coblentz Bag Co.,
Inc.,

Plaintiffs,

-against-

Norman N. Barnett, Julianne
Barnett and Vi L. Messerli,

Defendants.

File No. 76 Civ. 1994
(CLB)

NOTICE OF MOTION
TO DISMISS

-----X
Sirs:

Please take notice that upon the complaint dated
May 3, 1976, the undersigned, will move this court at a
Term for Motions to be held before the Hon. Charles L. Brieant,
Jr., in Court Room 501 of the United States Courthouse, Foley
Square, New York, New York on July 2, 1976 at 10:00 am., or as
soon thereafter as counsel can be heard, for an order pursuant
to Rules 9 and 12 of the Federal Rules of Civil Procedure,
dismissing the complaint and the action herein upon the
following grounds:

1. The complaint fails to state a claim within the
meaning of Rule 10b-5 and Section 10b of the Securities and
Exchange Act of 1934, as amended;
2. The complaint fails to plead fraud with
particularity;

Notice of Motion

3. The court lacks jurisdiction over the subject matter; and

4. The court lacks jurisdiction over the pendent claims for want of a valid federal claim to support the pendent jurisdiction;

and for such other and further relief as the court may seem just and proper.

Dated: New York, New York
June 14, 1976

Yours, etc.,

Eaton, Van Winkle & Greenspoon

By /s/ Samuel N. Greenspoon

(A Member of the Firm)

Attorneys for Defendants

Norman N. Barnett and

Julienne Barnett

Office and P. O. Address

600 Third Avenue

New York, New York 10016

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To: Carro, Spanbock, Londin,
Rochman & Fass
Attorneys for Plaintiffs
10 East 40th Street
New York, New York 10016

Complaint

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

-----X
MAXIME C. BARETGE, ROCKLEY ASSOCIATES, S.A., :
PIERRE MACHERAS; DAVID W. TRIMBLE; THE :
ROCKLEY GROUP, INC.; LA BAZOCHE, INC., :
WALBORG CORPORATION; and COBLENTZ BAG CO., :
INC., :

Plaintiffs, :

- against - :

NORHAN N. BARNETT, JULIENNE BARNETT :
and VI L. MESSERLI, :

Defendants. :
-----X

Index No.

76 Civ. _____

COMPLAINT

Plaintiffs, MAXIME C. BARETGE, ROCKLEY ASSOCIATES, S.A., PIERRE MACHERAS, DAVID W. TRIMBLE, THE ROCKLEY GROUP, INC., LA BAZOCHE, INC., WALBORG CORPORATION, and COBLENTZ BAG CO., INC., complaining of the defendants by their attorneys, CARRO, SPANBOCK, LONDIN, RODMAN & FASS, allege:

Jurisdiction

1. This action arises out of violations of Rule 10b-5, 17 CFR §240.10b-5, promulgated by the Securities and Exchange Commission under §10(b) of the Securities Exchange Act of 1934, 15 U.S.C. §78j(b). The Court has jurisdiction of the subject matter pursuant to §27 of said Act, 15 U.S.C. §78aa, and pendent jurisdiction. Alternatively, the Court has jurisdiction of the subject matter of Counts I and II because of the diversity of citizenship of the parties and jurisdictional amount under 28 U.S.C. §1332.

The Parties

2. Each of the individual plaintiffs is an alien:

(a) Plaintiff MAXIME C. BARETGE ("BARETGE"), is a citizen of France, and the nominee of plaintiff ROCKLEY ASSOCIATES, S.A., a Panamanian corporation ("ASSOCIATES"). BARETGE and ASSOCIATES, between them are record or beneficial owners of approximately 2,540 shares of the capital stock

Complaint

of plaintiff THE ROCKLEY GROUP, INC., ("ROCKLEY"), comprising approximately 25.4% of the stock of ROCKLEY which was issued and outstanding as of March 29, 1976. At all relevant times BARETGE has been and now is a director of ROCKLEY.

(b) Plaintiff PIERRE MACHERAS ("MACHERAS") is a citizen of France and is the record or beneficial owner of 1,000 shares of the capital stock of ROCKLEY, comprising approximately 10% of the stock of ROCKLEY which was issued and outstanding as of March 29, 1976. At all relevant times Francois Macheras, son of the plaintiff, has been and now is said plaintiff's designee on the board of directors of ROCKLEY.

(c) Plaintiff DAVID W. TRIMBLE ("TRIMBLE") is a British subject and is the record or beneficial owner of 650 shares of the capital stock of ROCKLEY, comprising approximately 6.5% of the stock of ROCKLEY which was issued and outstanding as of March 29, 1976. At all relevant times TRIMBLE has been and now is a director of ROCKLEY.

3. Plaintiff ROCKLEY is a Delaware corporation with its principal place of business in the City, County and State of New York, within the Southern District of New York. ROCKLEY is a holding company the sole business and assets of which is ownership of 100% of the issued and outstanding stock of plaintiff LA BAZOCHE, INC. ("LA BAZOCHE"). ROCKLEY also owns other inactive shell corporations.

4. Plaintiff LA BAZOCHE is a New York corporation with its principal place of business in the City, County and State of New York, within the Southern District of New York. LA BAZOCHE is a holding company, the sole business and assets of which is the ownership of all of the issued and outstanding stock of two operating corporations; plaintiff WALBORG CORPORA-

Complaint

TION ("WALBORG") and plaintiff COBLENTZ BAG CO., INC. ("COBLENTZ"), also a New York corporation.

5. Plaintiff WALBORG CORPORATION is a New York corporation with its principal place of business in the City, County and State of New York, and within the Southern District of New York.

6. Plaintiff COBLENTZ BAG CO., INC., is a New York corporation with its principal place of business in the City, County and State of New York, and within the Southern District of New York.

7. Upon information and belief, each of the defendants is a citizen of the State of New York, residing within the Southern District of New York:

(a) Defendant NORMAN N. BARNETT ("BARNETT") is a citizen of the United States and of the State of New York, residing at 45 East 89th Street, in the City and State of New York. Prior to March 29, 1976, BARNETT was the beneficial owner of approximately 5,135 shares of the capital stock of ROCKLEY and the record owner of an additional 400 shares, together comprising approximately 51% of the outstanding stock of ROCKLEY; a director and president of ROCKLEY; the sole voting trustee of all of the issued and outstanding stock of plaintiff LA BAZOCHE, and the sole director and president thereof; a beneficiary and controlling person of an offshore trust which controlled the stock of ROCKLEY beneficially owned by BARNETT, or by members of his family, including defendant JULIENNE BARNETT; was a director (at times the sole director) and president of WALBORG; and a director (at times the sole director) and president of COBLENTZ.

(b) Upon information and belief, defendant JULIENNE BARNETT, the wife of defendant BARNETT, is a citizen

Complaint.

of the United States and of the State of New York, residing at 45 East 89th Street, in the City and State of New York. From on or about March 11, 1975 to March 1, 1976, defendant JULIENNE BARNETT was a director of WALBORG, and from July 15, 1975 to March 1, 1976, said defendant was a director of COBLENTZ.

(c) Upon information and belief, defendant VI L. MESSERLI ("MESSERLI") is a citizen of the United States and of the State of New York, residing at 133 East 18th Street, in the City and State of New York. From on or about September 14, 1974 to March 16, 1976, defendant MESSERLI had been hired by defendant BARNETT in some unspecified "executive" capacity with ROCKLEY, and at various times said defendant held herself out to be an officer of ROCKLEY or its subsidiaries.

8. The amount in controversy exceeds \$10,000, exclusive of interest and costs.

COUNT I

(Individual plaintiffs against defendant Norman N. BARNETT)

9. Defendant BARNETT violated Rule 10b-5 promulgated by the Securities and Exchange Commission under §10(b) of the Securities Exchange Act of 1934, 15 U.S.C. §78j(b), by misrepresenting and omitting to state material facts in connection with the purchase or sale of securities, such violations being committed by the use of the United States Mails and the means and instrumentalities of interstate commerce, including the New York Clearing House.

10. The said violations of Rule 10b-5 by defendant BARNETT included the making of untrue statements of material fact and the omission to state material facts necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading in

Complaint

connection with the purchase and sale of securities by the use of the means and instrumentalities of interstate commerce and the mails; the employment of devices, schemes or artifices to defraud, and engaging in acts, practices and courses of business which operated as a fraud and deceit upon the individual plaintiffs BARETGE, MACHERAS, TRIMBLE and ASSOCIATES by inducing said plaintiffs to invest their moneys in and purchase securities of corporations which defendant BARNETT intended to loot and did loot, and when said corporations were threatened with imminent foreclosure and bankruptcy as a result of said defendant's depredations, reselling control of said corporations to the individual plaintiffs and coercing them to issue general releases to defendants BARNETT and JULIENNE BARNETT, without making suitable disclosures as to what the several plaintiffs were being asked to release.

11. In or about late 1973 plaintiff BARETGE, a businessman residing in Barbados, was looking for a vehicle for investment by himself and some business associates, including the other individual plaintiffs, in American businesses engaged in the importation and marketing into the United States of high fashion consumer products. BARETGE hoped that if such an enterprise were successful it could eventually form the basis for a public offering of securities.

12. BARETGE had known defendant BARNETT for a number of years. BARNETT had previously been affiliated with various monied institutions and had had the management of large amounts of capital. BARNETT represented to BARETGE that he had the knowledge and managerial experience to operate the sort of enterprise which BARETGE had in mind. He also told BARETGE that he was himself looking for an "off shore" vehicle with which to shelter his own income.

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13. Accordingly it was agreed between BARETGE and BARNETT that the defendant would look for suitable investment opportunities of the kind discussed, BARETGE and his associates would supply most of the necessary initial funds, and BARNETT would supply the knowledge and managerial abilities which he represented he had. It was agreed that after the additional initial investors had been given their shares in the enterprise, plaintiff BARETGE and defendant BARNETT would own equal amounts of stock therein, and have equal voice in policy decisions, and BARNETT so represented to the other individual plaintiffs before they invested in ROCKLEY.

14. Upon information and belief, at or about this time defendant BARNETT conceived and formulated a scheme by which he would obtain for himself the control of the contemplated business venture by creating a complex of corporate and trust entities (which he represented were necessary in order to achieve the goals both of BARETGE and his associates, and of BARNETT) to conceal the scheme, and having achieved control he would convert to his own use the income and assets of the businesses acquired with funds of BARETGE and his associates.

15. In early 1974 defendant BARNETT learned of the existence and availability of WALBORG, an importer and distributor of high fashion products for women. He thereupon entered into negotiations with Richard and Hilde Walborg Weinberg, who were the sole stockholders of WALBORG, for the acquisition of all of the capital stock of WALBORG. On or about April 26, 1974, BARNETT, who had just arranged for the incorporation of plaintiff LA BAZOCHE---on behalf of BARETGE, plaintiff TRIMBLE and himself---agreed with the Weinbergs to purchase all of the issued and outstanding stock of WALBORG

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for a total price of \$860,000, payment of which was to be made as follows: approximately \$250,000 to be paid in cash at or about the time of the closing; the balance to be paid over a period of time. Of the purchase price which was required to be deposited, \$82,111.64 was supplied by plaintiff BARETGE, and LA BAZOCHE borrowed the balance from the First National City Bank of New York ("Citibank"), to which it gave its note for \$600,000. The note was personally guaranteed by defendant BARNETT, although, on information and belief, he knew that he had no reasonable prospect of being able to honor his guarantee if called upon to do so by Citibank.

16. As part of his fraudulent scheme to secure for himself complete control of WALBORG (and of any other operating companies later to be acquired), and in breach of his fiduciary duties to BARETGE and his associates in whose behalf he was negotiating with the Weinbergs, defendant BARNETT arranged for the incorporation of a second corporation, which became ROCKLEY, to hold beneficial title to the stock of LA BAZOCHE. The true purpose of such incorporation was to interpose another entity between the individual plaintiffs and LA BAZOCHE. BARNETT falsely represented to the individual plaintiffs that the formation of ROCKLEY was necessary and that its sole purpose, as a matter of law, was to insulate the individual plaintiffs from any of LA BAZOCHE's liabilities. In addition, dealing with himself, defendant BARNETT, who was then the sole record stockholder and sole director of LA BAZOCHE, entered into a ten year voting trust agreement with respect to all of the voting stock of LA BAZOCHE, pursuant to which he would have complete and exclusive control of the operating companies purchased by LA BAZOCHE in major part with funds supplied by BARETGE. In the circumstances, these

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virtually simultaneous transactions were acts, practices and courses of business which operated and were intended to operate as a fraud and deceit upon plaintiff BARETGE and his business associates and prospective investors, the other individual plaintiffs.

17. Furthermore, in acquiring all of the stock of Walborg for LA BAZOCHE, i.e., for BARETGE and his associates, defendant BARNETT made a number of misrepresentations of material fact for the purpose of gaining for himself personal control of WALBORG, free from the interference of the individual plaintiffs as investors in, and prospective directors of, the holding company which was to own the stock of WALBORG.

(a) Defendant BARNETT represented to the Weinbergs that he was the sole voting trustee of a ten year irrevocable voting trust agreement dated April 25, 1974, among the holders of all of the issued and outstanding stock of LA BAZOCHE, pursuant to which he had "the sole and exclusive voting rights of all of the issued and outstanding shares of capital stock of" LA BAZOCHE, and also that "he has advised each and every one of the beneficial owners of the outstanding capital stock of [LA BAZOCHE] of the terms and conditions of [the purchase agreement] and has obtained their consent to" such terms; and that the voting trust agreement was the Weinbergs' best assurance that LA BAZOCHE would duly perform all of the pay-out provisions of the stock purchase agreement. These representations were false and misleading and were known by defendant BARNETT to be false when he made them, because the sole purpose for the voting trust agreement was to obtain control of WALBORG for BARNETT, adversely to the interests of the individual plaintiffs as investors, and to the interests of the Weinbergs as sellers of the stock of WALBORG, and, at

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the time it was made, there were no beneficial stockholders of LA BAZOCHE. Even if BARETGE were deemed to be a beneficial owner of LA BAZOCHE because he had contributed \$82,111.64 for LA BAZOCHE'S down payment for the stock of WALBORG, he had neither known of any voting trust agreement beforehand, nor given his consent thereto.

(b) After having persuaded the Weinbergs that the voting trust agreement was indispensable for their own protection, defendant BARNETT falsely represented to plaintiff BARETGE that the Weinbergs themselves had suggested and insisted upon the execution of the voting trust agreement for their own protection, and that they would not have entered into the agreement for the sale of their stock in WALBORG unless BARNETT himself was in a position to guarantee their right to pay-outs under the agreement. Defendant BARNETT also represented to BARETGE that BARETGE's interests would not be adversely affected by the voting trust agreement. Said representations were false in material respects, and were known by BARNETT to be false when he made them.

18. Prior to the incorporation of LA BAZOCHE and ROCKLEY, defendant BARNETT falsely represented to the plaintiffs that it was necessary to create two corporations in order to insulate plaintiffs from any liabilities which the purchasers of WALBORG would be obliged to assume. To induce the individual plaintiffs BARETGE, MACHERAS, and TRIMBLE to purchase securities, defendant BARNETT represented to them, on or about April 15, 1974, that the business and earnings of WALBORG, then ROCKLEY's (or LA BAZOCHE's) only operating subsidiary, were such that "the deal can be bootstrapped almost entirely on the basis of Walborg's net assets and historical earnings," which would result in ROCKLEY's being a company with:

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"a residual (i.e., after taking into account bank debt and deferred principal payments 'taken back' by the sellers) tangible net worth of approximately \$750K;

"a capitalized earnings value in excess of \$2MM based on reconstructed P & L historical results (Walborg has never lost money since it was founded 23 years ago); and

"a conservatively projected cash flow adequate to cover all deferred payments to the sellers and full amortization of the bank loan, on schedule, over 5 years."

19. Defendant BARNETT also misrepresented to the individual plaintiffs, and each of them, that "Max [i.e., BARETGE] and I will be in overall charge" of the operations to be controlled by the holding company, ROCKLEY, whereas defendant BARNETT intended to secure for himself the full control of ROCKLEY, LA BAZOCHE and WALBORG.

20. In a unanimous consent in lieu of an organizational meeting of ROCKLEY dated June 11, 1974, stock of ROCKLEY was issued, inter alia to the individual plaintiffs and defendant BARNETT, for the considerations, recited below:

(a) To plaintiffs BARETGE and/or S.A., 700 shares of ROCKLEY capital stock, 300 shares in consideration of services rendered by BARETGE and valued at \$75,000, and 400 shares for cash paid or to be paid on or before July 31, 1974 in the aggregate amount of \$100,000.

(b) To plaintiff TRIMBLE, 550 shares of ROCKLEY capital stock, 150 shares in consideration of services rendered by TRIMBLE and valued at \$37,500, and 400 shares for cash theretofore paid or to be paid at the time of the issuance of the shares and cash to be paid on demand in the aggregate amount of \$100,000.

(c) To plaintiff MACHEMAS, 1,000 shares of ROCKLEY capital stock in consideration of cash to be paid

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at the time of the issuance of such shares in the aggregate amount of \$250,000.

(d) To defendant BARNETT, 6,700 shares of ROCKLEY capital stock in consideration of (i) services rendered by BARNETT and valued at \$75,000; (ii) the transfer to ROCKLEY of the beneficial ownership of all of the issued and outstanding stock of LA BAZOCHE, the fair value of which was represented to be \$1,440,000; (iii) the transfer to ROCKLEY of 2,000,000 shares of the common stock of Belmont Industries, Inc., a publicly-held Delaware corporate shell the fair value of which was represented by BARNETT to be \$60,000; (iv) cash which BARNETT represented had theretofore allegedly been paid by him to or for the benefit of ROCKLEY in the amount of \$20,222.96; and (v) cash which BARNETT represented he would pay on or before July 31, 1974 in the amount of \$79,777.04; or a total stated consideration paid or to be paid by defendant BARNETT of \$1,675,000.

21. Whereas the "unanimous consent"---which had been prepared by BARNETT---correctly recited the several considerations received or to be received from the individual plaintiffs for the issuance of stock to them, its recitations of defendant BARNETT's actual or promised contributions to ROCKLEY were grossly overstated or illusory, and were known by BARNETT to be false when made. Defendant BARNETT misrepresented the facts in that:

(a) The beneficial ownership of all of the issued and outstanding stock of LA BAZOCHE, for which defendant BARNETT gave himself a credit of \$1,440,000, had been acquired by him as nominee for the individual plaintiffs, with plaintiff BARETGE contributing \$82,111.64 in cash, and the remainder of the initial down payment being made by a bank loan to LA

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BAZOCHE itself, secured by a worthless guarantee by defendant BARNETT.

(b) The 2,000,000 shares of Belmont Industries, Inc., valued by BARNETT at \$60,000, were never in fact contributed to ROCKLEY because the deal by which BARNETT was to have acquired such shares was never consummated.

(c) The aggregate of \$100,000 in cash which defendant BARNETT claimed to have contributed or was to contribute, was, on information and belief never invested in ROCKLEY or its subsidiaries by said defendant.

22. Defendant BARNETT's representations to the individual plaintiffs respecting the manner in which he intended to conduct the business of ROCKLEY were false when made, and in addition said defendant omitted to inform said plaintiffs that he would use the assets of ROCKLEY, to wit: the income generated by its then sole operating subsidiary, WALBORG, for his own personal use and benefit, supply himself and other employees of ROCKLEY, LA BAZOCHE and WALBORG with extravagant automobiles and vacations in Europe (including a trip to Cannes, France, for the wedding of plaintiff BARETGE, at which time the "unanimous consent" was executed); fail and neglect to make timely payments of the pay-out instalments due the Weinbergs, and timely repayments of the instalments of principal and interest which would become due on LA BAZOCHE's bank loans which had been made in connection with its purchase of the stock of WALBORG, thereby jeopardizing its credit and threatening the solvency of the overall enterprise beneficially owned by ROCKLEY, and through it, by the plaintiffs.

23. The individual plaintiffs did not know, at the time or times these representations were made that they were false in material respects, and in the exercise of reasonable diligence, they could not have learned the true facts:

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(a) The individual plaintiffs could not have known that the genesis of the voting trust agreement originated with defendant BARNETT (and not with the Weinbergs) since defendant BARNETT had conducted the entire negotiations with the Weinbergs. Plaintiffs had no reason to doubt defendant's statement that the Weinbergs themselves had insisted on a voting trust, or to assume that the idea had first been suggested by the defendant.

(b) As respects defendant BARNETT's express or implied representation that his personal guarantee of the bank loans utilized to pay the down payment for the stock of WALBORG was indispensable to the Citibank's agreeing to make the loans, and that his guarantees had value, plaintiffs did not know or have reason to believe that such guarantees either had not been insisted upon by Citibank, or that they were worthless because defendant could not honor them if called upon to do so, or both.

(c) At the time of these transactions, it was not obvious as it now is that, for no capital investment of his own, BARNETT had acquired for himself a majority of the capital stock of ROCKLEY, which, when taken together with the voting trust agreement covering all of the stock of LA BAZOCHE beneficially owned by ROCKLEY, gave him complete control of the assets and business of ROCKLEY and its subsidiaries. At the time plaintiffs did not realize that BARNETT's guarantees to Citibank were in fact worthless and unnecessary; that he claimed credit for himself of the entire capitalized earnings of WALBORG and not merely the cash purchase price of its stock; and that he had neither invested the cash or other assets as represented, nor had either the ability or the intention of doing so.

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24. The acts of defendant BARNETT and the representations which he had made to the individual plaintiffs BARETGE, MACHERAS (through his son and attorney-in-fact, Francois Macheras) and TRIMBLE were knowingly and intentionally false and deceptive, and omitted to state material facts; were made in connection with the purchases and sales of securities and by the use of the mails and instrumentalities of interstate commerce; and were intended to defraud and had the effect of defrauding the said plaintiffs into giving defendant BARNETT an equity position in ROCKLEY grossly disproportionate to his actual contributions of capital, services or experience; and were in complete breach of the fiduciary duties which said defendant had assumed to plaintiffs as their nominee and agent in acquiring the voting stock of Walborg and the creation of LA BAZOCHE. The aforesaid misrepresentations and omissions of material facts were also accompanied by, and concealed through, the use of devices, schemes and artifices to defraud, including interlocking stock ownership relationships, which made it difficult, if not impossible, to ascertain BARNETT's true role in the complex of companies.

25. Had the individual plaintiffs known the true facts, they would not have invested in ROCKLEY upon the terms and under the circumstances which defendant BARNETT's representations induced them actually to invest.

COUNT II
(Plaintiffs BARETGE, TRIMBLE and ASSOCIATES against defendant
Norman N. BARNETT)

26. Plaintiffs repeat and incorporate herein by reference as though fully set forth, each and every allegation contained in paragraphs of this Complaint numbered 1 through 25, inclusive.

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27. Despite repeated requests from each of the individual plaintiffs, as stockholders in and as directors of ROCKLEY, defendant BARNETT repeatedly failed and refused to provide plaintiffs with up-to-date financial statements respecting the operations of ROCKLEY and its subsidiaries, falsely explaining that they were not available because of computer problems at IBM.

28. Nevertheless, despite the absence of current financial statements, defendant BARNETT represented to the individual plaintiffs, at a meeting of the board of directors of ROCKLEY held in New York City on or about December 6, 1975, that the business of ROCKLEY and its subsidiaries was doing well, and that WALBORG would achieve a turnover of \$4.1 million, while COBLENTZ (the second operating subsidiary of LA BAZOCHE which was acquired on or about July 1, 1975 in part with a loan from Citibank, would achieve a turn-over of \$1.6 million, and that the 1976 figures would exceed the 1975 profit margins. Defendant BARNETT represented to the plaintiffs that the Citibank and The Chase Manhattan Bank, N.A. ("Chase"), which had extended a line of credit to ROCKLEY and its subsidiaries, were concerned with the high debt-to-equity capitalization of ROCKLEY and wanted a capital contribution to ROCKLEY to improve the ratio.

29. Upon information and belief, these representations by defendant BARNETT were false when made, and were known by him to be false. In fact, ROCKLEY had prepared or received unaudited financial statements on a consolidated basis at least quarterly. Upon information and belief, the aggregate turn-overs for WALBORG and COBLENTZ for the period covered by defendant BARNETT's misrepresentation was approximately \$5.1 million, an amount approximately 11% less than

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that represented by defendant BARNETT to the individual plaintiffs; and the banks had not insisted on a greater capital investment in ROCKLEY or complained of the equity-to-debt ratio.

30. The said misrepresentations were made by defendant BARNETT in order to induce the plaintiffs to contribute additional capital to ROCKLEY by way of purchases of additional stock. In response to the said misrepresentations, which involved the use of the U.S. Mails and the instrumentalities of interstate commerce, on or about December 15, 1975, plaintiff BARETGE caused plaintiff ASSOCIATES to invest an additional \$150,000 in ROCKLEY, for which ASSOCIATES received an additional 1,840 shares of ROCKLEY capital stock. Between January and March 1976, plaintiff TRIMBLE invested an additional \$37,500 in ROCKLEY, for which he also received shares of ROCKLEY's capital stock.

31. Upon information and belief, defendant BARNETT appropriated to his own use a significant portion of the new investment made in ROCKLEY by plaintiffs BARETGE, TRIMBLE and ASSOCIATES, while the bulk of the investment was spent on the repayment of liabilities of ROCKLEY and its subsidiaries which BARNETT had failed to disclose to the plaintiffs and had implicitly denied existed.

32. Had plaintiffs BARETGE and TRIMBLE known the true facts, they would not have made the additional investments or, in the case of plaintiff BARETGE, would not have caused ASSOCIATES to do so.

COUNT III

(The corporate plaintiffs against defendants NORMAN N. BARNETT, JULIENNE BARNETT and VI L. HESSERLI)

33. Plaintiffs repeat and incorporate herein by reference each and every allegation contained in paragraphs 1 through 8, and 10 through 25, inclusive, of this Complaint.

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34. Upon information and belief, during the period commencing with the incorporation of ROCKLEY and LA BAZOCHE on and after April 25, 1974, defendant BARNETT, in furtherance of his fraudulent scheme and in breach of his fiduciary duties to all plaintiffs---as the nominee of the individual plaintiffs, as majority shareholder, president and director of ROCKLEY, as sole voting trustee and sole director of LA BAZOCHE, and as sole or controlling director and president of WALBORG and COBLENTZ---converted to his own use and stole assets and moneys belonging of right to ROCKLEY or its said subsidiaries in amounts which plaintiffs believe exceeded \$500,000, in the aggregate. In addition to appropriating assets to his own use, defendant BARNETT gave to friends, associates, and co-conspirators, including his wife, defendant JULIENNE BARNETT and defendant MESSERLY, gifts of corporate property, or loans or excessive salaries or excessive payments for services allegedly rendered or to be rendered, such salaries and payments being grossly disproportionate to the actual value of the services actually performed for or received by any such corporation, including the following:

(a) Prior to the acquisition of WALBORG, defendant BARNETT purported to incur necessary travel expenses of approximately \$35,000 per year. During the calendar year 1975, the travel expenses billed by said defendant to ROCKLEY or its subsidiaries were approximately \$150,000.

(b) Between April 1974 and December 31, 1974, defendant BARNETT withdrew between \$60,000 and \$75,000 out of the income and earnings of ROCKLEY or its subsidiaries, said amounts being over and above any amounts which were lawfully due to defendant under his employment contract or otherwise, and such withdrawals being neither known to the Board of Directors of ROCKLEY nor authorized by it.

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(c) On or about October 1, 1974, without the knowledge or approval of the Board of Directors of ROCKLEY (i.e., of the sole stockholder of LA BAZOCHE), and in violation of New York Business Corporation Law § 714, defendant BARNETT borrowed \$30,000 from LA BAZOCHE, for which he gave it his unsecured promissory note bearing interest at the rate of 8% per annum, and payable on June 30, 1979. At that time defendant BARNETT prepaid the interest to December 31, 1975 out of the proceeds of the unlawful loan.

(d) During calendar year 1975, defendant BARNETT withdrew approximately \$71,000 more from the income or assets of ROCKLEY and its subsidiaries, said amounts also being in excess of any amounts lawfully due the defendant, and the withdrawals having been made without the knowledge and prior approval of the Board of Directors of ROCKLEY.

(e) During the first three months of 1976, BARNETT withdrew an aggregate of \$33,000 from the income or assets of ROCKLEY and its subsidiaries, including a payment of \$8,000 to his wife, defendant JULIENNE BARNETT, while representing to plaintiffs that he had taken virtually no salary in 1976, and that his said wife had received no payments.

(f) During calendar years 1974 and 1975, defendant BARNETT took his family to Europe twice at the expense of ROCKLEY, and while in Greece in 1975 he chartered a yacht at ROCKLEY's expense. Neither the trips to Europe nor the yacht charter were known to or authorized by the Board of Directors of ROCKLEY.

(g) Although defendant BARNETT was entitled by his employment agreement to be provided with an automobile at the expense of ROCKLEY, he caused ROCKLEY to purchase at least two and probably three Mercedes Benz and one Porsche

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automobiles, for an aggregate purchase price in excess of \$50,000, and to pay for said automobiles defendant BARNETT caused ROCKLEY to borrow the funds from The Chase Manhattan Bank, N.A. ("Chase"). Neither the acquisition of cars of such luxury and expense, nor the number so acquired, was known to or authorized by the Board of Directors of ROCKLEY, and the Board neither knew of nor authorized the borrowing of funds for such purpose.

(h) Upon information and belief, in 1974 and 1975, defendant BARNETT caused WALBORG to borrow against, and then converted to his own use some or all of the \$106,000 proceeds of the cash value of "key man" insurance policies on the lives of Mr. and Mrs. Weinberg, which policies were owned and the premiums thereon paid for by WALBORG.

(i) Upon information and belief, in February 1976, defendant BARNETT sold one of the Mercedes Benz automobiles referred to above, for \$10,000, a price substantially below its true value, and deposited the purchase price thereof in a corporate bank account of ROCKLEY or one of its subsidiaries which was unknown to and unauthorized by the board of directors of ROCKLEY. Defendant BARNETT thereafter converted and appropriated to his own use the proceeds of said sale.

(j) On or about March 1, 1976, just before defendant BARNETT began negotiations with the individual plaintiffs relating to his resignation from the ROCKLEY group of companies, defendant BARNETT, without the knowledge or consent of the Board of Directors of ROCKLEY, and in violation of § 143 of the Delaware General Corporation Law, borrowed \$15,000 from ROCKLEY, giving an unsecured, non-interest bearing demand note therefor. Although demand for payment thereof has been made, payment has not been received.

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(k) On or about February 27, 1976, again without the knowledge or consent of the Board of Directors of ROCKLEY, defendants BARNETT and MESSERLI caused ROCKLEY to transfer to BARNETT, without consideration to ROCKLEY, title to a "key man" life insurance policy on his own life, in the face amount of \$1,000,000 having a cash surrender value of approximately \$35,000, which had been purchased and the premiums on which had been paid by ROCKLEY. Upon information and belief, the documents transferring ownership of the policy to defendant BARNETT were executed on behalf of ROCKLEY by defendants BARNETT and MESSERLI, who signed herself as Vice-President for Production and Planning, although she was not an officer. On or about February 28, 1976, defendant BARNETT transferred the ownership of the said life insurance policy to his wife, defendant JULIENNE BARNETT, who was at the time a director of WALBORG and continued as such until March 1, 1976 when she resigned.

(l) Upon information and belief, also during February 1976, at about the time defendant MESSERLI was lending her name as putative officer of ROCKLEY to the fraudulent transfer to BARNETT of the insurance policy on his life, and just prior to his disclosure to plaintiffs that LA BAZOCHE was involved in a "liquidity crisis", BARNETT unilaterally increased the salary of MESSERLI from \$14,000 per annum with additional perquisites, to \$26,000 per annum.

(m) Upon information and belief, in June and November 1975, defendant BARNETT used corporate funds of ROCKLEY and WALBORG to make two unsecured loans aggregating \$20,000 to defendant MESSERLI. Such loans were made without the knowledge or approval of the Board of Directors of ROCKLEY, and were not made for any legitimate corporate purpose of ROCKLEY

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or WALBORG. They thus violated the Delaware General Corporation Law and the New York Business Corporation law, respectively, and were made at a time or times when defendant BARNETT was soliciting additional capital contributions from the individual plaintiffs. On or about October 1, 1975, defendant HESSERLI gave ROCKLEY her note for \$20,000 with 8% interest, payable to ROCKLEY on June 30, 1979. Thereafter, on or about on or about January 2, 1976, again without the knowledge or approval of the Board of Directors of ROCKLEY, and without any consideration therefor to ROCKLEY, defendant BARNETT purported to cancel, and returned to defendant HESSERLI, the note which she had given ROCKLEY as evidence of her indebtedness.

(n) Upon information and belief, defendant BARNETT failed and neglected, as chief executive officer of ROCKLEY and its subsidiaries, to cause each of those corporations to pay withholding taxes to the United States Government and other taxing authorities with respect to additional monetary and other benefits which said defendant appropriated to himself from such companies, thereby exposing ROCKLEY and its said subsidiaries to liability to the Government and the other taxing authorities, for the payment of withholding tax in amounts not presently determinable, and interest and penalties thereon.

35. By reason of her position as a director of WALBORG, defendant JULIENNE BARNETT knew or should have known that the transfer to her by defendant BARNETT of an insurance policy which was the property of WALBORG was wrongful and fraudulent, and the putative transfer of ownership of said policy to said defendant JULIENNE BARNETT should be adjudged to be null, void and of no effect, such transfer should be

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set aside as fraudulent as against ROCKLEY, and defendant JULIENNE BARNETT adjudged liable to return said policy, or the proceeds of its disposal to ROCKLEY.

36. Defendant MESSERLI knew or should have known that the purported forgiveness by defendant BARNETT of a \$20,000 note, the equivalent of approximately seventeen months salary, was unauthorized, violated the Delaware General Corporation Law, and fraudulent as to ROCKLEY, and was done and the Court should enter judgment setting aside the cancellation of said note as fraudulent as against WALBORG and/or ROCKLEY, declaring defendant MESSERLI to be justly indebted to said corporation or corporations, and requiring defendant MESSERLI to repay ROCKLEY forthwith.

37. On or about May 1, 1976, defendant MESSERLI commenced an action in the New York State Supreme Court against plaintiffs ROCKLEY, LA BAZOCHE and WALBORG, claiming, contrary to the written terms of her agreement, that she was employed from year to year and that the termination of her employment by ROCKLEY on or about March 31, 1976 was a breach of her employment agreement, seeking injunctive relief directing the said plaintiffs to continue her on the payroll through September 1976 at a salary of \$26,000 per annum. The motion for a preliminary injunction was supported by an affidavit of her co-conspirator, defendant BARNETT. The Court should enter judgment declaring that defendant MESSERLI was an employee at will subject to dismissal at will, that she was properly dismissed, that the increase of her salary from \$14,000 to \$26,000 per annum was fraudulent and improper, and awarding judgment against her for any amounts in excess of the lower rate which she received as salary.

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38. By reason of his gross breaches of fiduciary duties owing to the several corporate plaintiffs, and particularly ROCKLEY, LA BAZOCHE and WALBORG, defendant BARNETT should be surcharged the amount of all improper and fraudulent withdrawals made by him of the assets or moneys of each such corporation.

COUNT IV

(All plaintiffs against defendants NORMAN N. BARNETT, JULIENNE BARNETT and VI L. MESSERLI)

39. Plaintiffs repeat and incorporate herein by reference each and every allegation contained in paragraphs 1 through 25, 27 through 32, and 34 through 38, inclusive, of this Complaint.

40. As president of ROCKLEY and of its several subsidiary corporations, and as sole director of some of the subsidiaries, defendant BARNETT attempted to prevent the individual plaintiffs from exercising their fiduciary responsibilities by failing to keep them informed of corporate developments, and by demanding, in early March 1976, that they leave the premises of WALBORG where they were attempting to ascertain the true financial condition of that company.

41. Upon information and belief, on or about March 22, 1976, Citibank notified BARNETT that LA BAZOCHE was in default with respect to its loans, and that on March 26, 1976 Citibank would commence legal action to foreclose its loan. Upon information and belief, at about the same time Chase also notified BARNETT that unless LA BAZOCHE's indebtedness to it, which had been incurred in connection with its letter of credit and the acquisition of the automobiles was immediately paid, it too would commence legal proceedings.

42. On March 26, 1976, after intensive night long negotiations following a week of meetings, plaintiffs and

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defendant BARNETT entered into a settlement agreement by which defendant BARNETT would resign all his positions with the ROCKLEY group of companies, would surrender all his stock therein (including stock in ROCKLEY which he had caused to be transferred to members of his family, including defendant JULIENNE BARNETT, or which was beneficially owned by him or by the said JULIENNE BARNETT, would be permitted to purchase one of the Mercedes Benz automobiles and also would receive \$60,000 over a period of months (less any withholding taxes, interest or penalties due the federal New York State and New York City governments with respect to BARNETT's own withdrawals).

43. As a condition of his agreeing to withdraw from the management of ROCKLEY and its subsidiaries and to surrender any securities owned of record or beneficially by him or his family, defendant BARNETT insisted that each of the individual plaintiffs and each of the corporate plaintiffs of which he had been a fiduciary give him and his wife, defendant JULIENNE BARNETT, a general release, which all of the plaintiffs were obliged to agree to since they in good faith believed that BARNETT would permit the corporate plaintiffs to be driven into bankruptcy. During the course of these lengthy negotiations, the books and records of the several corporate plaintiffs were kept in BARNETT's own apartment and not in the corporate offices, and plaintiffs therefore could not ascertain the foregoing facts, most of which they discovered only after executing the settlement agreement of March 29, 1976 and the concurrent surrender of several file drawers of corporate records.

44. Having no other alternative to seeing their entire investment destroyed in bankruptcy, the individual

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plaintiffs agreed to grant individual and corporate releases to defendants BARNETT and JULIENNE BARNETT, having no idea that such wrongdoing as might have occurred was of the magnitude which they subsequently discovered it to be. In the circumstances, the omission of defendant BARNETT to state material facts in connection with his resale of his stock in ROCKLEY to the plaintiffs was in and of itself violative of Rule 10b-5, and the releases which he extorted from the individual and corporate plaintiffs should be set aside as fraudulent.

45. The acts of defendant BARNETT, including the acts involved in, or occurring during the period of, the negotiations leading to the settlement agreement of March 29, 1976, in addition to being in violation of said Rule 10b-5, involved fraud and deceit under the laws of the State of New York, and are the sort of acts for which an Order of Attachment may issue under New York Civil Practice Law and Rules §6201(4), (5) and/or (7).

46. Upon information and belief, defendant BARNETT has already assigned or secreted assets of ROCKLEY or its subsidiaries which he unlawfully and fraudulently converted to his own use, and, if an Order of Attachment be not granted forthwith, will assign or secrete such assets abroad, to prevent this Court's seizure of such assets.

WHEREFORE, plaintiffs MAXINE C. BARETGE, ROCKLEY ASSOCIATES, S.A., PIERRE MACHERAS, DAVID W. TRIMBLE, THE ROCKLEY GROUP, INC., LA DAZOCHE, INC., WALBORG CORPORATION, and COBLENTZ BAG CO., INC., demand judgment against defendants NORMAN N. BARNETT, JULIENNE BARNETT and VI L. HESSERLI, as the respective interests of the several plaintiffs may appear:

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(a) As to Counts I and II:

(1) Granting judgment as against defendant NORMAN N. BARNETT, and awarding to each of the plaintiffs, MAXIME C. BARETGE, ROCKLEY ASSOCIATES, S.A., PIERRE MACHERAS and DAVID W. TRIMBLE, the amount of the damages by him or it sustained as a result of defendant NORMAN N. BARNETT's wilful violation of Rule 10b-5 and common law fraud, and granting said plaintiffs an Order of Attachment against the assets and bank accounts of defendant Norman N. BARNETT.

(b) As to Counts III and IV:

(2) Granting plaintiffs THE ROCKLEY GROUP, INC., LA BAZOCHE, INC., WALBORG CORPORATON and COBLENTZ BAG CO., INC., an accounting of defendant NORMAN N. BARNETT's stewardship of the affairs of those corporations, and surcharging him and requiring him to reimburse each such corporation for all amounts unlawfully taken by said defendant in cash or perquisites, beyond amounts to which he was lawfully entitled under his contract of employment, and requiring said defendant to restore to said corporations all moneys and chattels which he may have converted to his own use, or the proceeds of the sale thereof, which are the property of any such corporation.

(3) Granting to the plaintiffs THE ROCKLEY GROUP, INC., LA BAZOCHE, INC., WALBORG CORPORATION, and COBLENTZ BAG CO., INC., an Order of Attachment against the assets and bank accounts of defendant Norman N. BARNETT.

(4) Adjudging said defendant NORMAN N. BARNETT liable to indemnify plaintiffs THE ROCKLEY GROUP, INC., LA BAZOCHE, INC., or their subsidiaries, and to hold same harmless with respect to any liabilities for withholding or other taxes, or any interest or penalties thereon, which may

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be charged against any such corporation by the United States Government or any other taxing authority on account of said defendant's having fraudulently appropriated to himself moneys and properties of any of said corporations which might be deemed additional income to him.

(5) Adjudging said defendant NORMAN N. BARNETT liable to reimburse plaintiffs THE ROCKLEY GROUP, INC. or LA BAZOCHE, INC., or their subsidiaries, for excess salaries and gifts of corporate funds given by said defendant to his friends or co-conspirators, ostensibly as salaries or as payment for services rendered to said corporations or their subsidiaries, to the extent that such payments of corporate funds were in excess of the value of the services received, if any, by either or both corporations or their subsidiaries; and in the case of loans to said defendant or to other officers of any such corporate plaintiff, to the extent that such loans were made without the knowledge or approval of the Board of Directors of ROCKLEY.

(6) Granting judgment to plaintiff THE ROCKLEY GROUP, INC., against defendants NORMAN N. BARNETT and JULIENNE BARNETT, declaring null, void and of no effect, and setting aside as fraudulent as against the rights of ROCKLEY the purported transfer, initially from ROCKLEY to defendant NORMAN N. BARNETT, and thereafter from that defendant to defendant JULIENNE BARNETT, of the ownership of an insurance policy owned by said ROCKLEY on the life of defendant NORMAN N. BARNETT; and directing the said defendant JULIENNE BARNETT to return to ROCKLEY the said insurance policy or any proceeds from the surrender thereof.

(7) Granting judgment to plaintiff THE ROCKLEY GROUP, INC., against defendant VI L. MESSERLI, declaring

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null, void and of no effect, and setting aside as fraudulent as against the rights of said plaintiff, the purported cancellation and surrender to said defendant MESSERLI of an evidence of indebtedness to said plaintiff in the amount of \$20,000; and adjudging said defendant MESSERLI to be justly indebted to plaintiff THE ROCKLEY GROUP, INC., in said amount.

(8) To the extent that defendant JULIENNE BARNETT may have received from defendant BARNETT any assets, moneys or other properties belonging to any of the corporate plaintiffs to which she was not lawfully entitled, granting an Order of Attachment against the assets and bank accounts of defendant JULIENNE BARNETT.

(9) Granting judgment to plaintiff THE ROCKLEY GROUP, INC., adjudging and declaring that defendant VIL MESSERLI was properly dismissed from her employment by said plaintiff; setting aside as fraudulent the purported increase in said defendant's salary from \$14,000 to \$26,000 per annum; awarding judgment to said plaintiff against said defendant for any amounts received by said defendant in excess of her contractual salary of \$14,000; and directing defendant MESSERLI to account to plaintiff THE ROCKLEY GROUP, INC., and its subsidiaries, for all amounts other than salaries which she received, and for all services which she allegedly performed on account of additional contractual payments of \$3,500 per annum.

(c) As to Count IV:

(10) Granting judgment to plaintiffs MAXIME C. BARETCE, PIERRE MACHERAS, DAVID W. TRIMBLE, ROCKLEY ASSOCIATES, S.A., THE ROCKLEY GROUP, INC., LA BAZOCHE, INC., WALBORG CORPORATION, AND COBLENTZ BAG CO., INC., judgment against defendants NORMAN N. BARNETT and JULIENNE BARNETT,

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declaring null, void and of no effect, and setting aside as fraudulently and coercively induced general releases executed by or on behalf of each such plaintiff on or about March 29, 1976, and running in favor of defendants NORMAN N. BARNETT and JULIENNE BARNETT.

(11) Granting judgment to plaintiff WALBORG CORPORATION against defendant NORMAN N. BARNETT, declaring null, void and of no effect, and cancelling the obligation of said plaintiff as fraudulently and coercively induced, to pay defendant NORMAN N. BARNETT the sum of \$60,000 over a period of time (less any amounts which may be found to be due to various taxing authorities on account of said defendant's failure to withhold taxes on account of his withdrawals).

(d) As to all Counts:

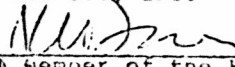
(12) To the extent that the wrongdoing of defendant NORMAN N. BARNETT is also violative of the laws of the States of New York and Delaware, as the case may be, awarding the individual plaintiffs and plaintiffs THE ROCKLEY GROUP, INC., LA BAZOCHE, INC., and WALBORG CORPORATION punitive or exemplary damages; and

(13) Awarding to each of the plaintiffs interest on any recovery from the date of each alleged wrongdoing, and the costs and disbursements of this action, and granting to each such plaintiff such other, further and different relief as to the Court may seem just and proper in the premises.

Dated: New York, New York
May 3, 1976

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By 
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CERTIFICATE OF SERVICE

REGINALD LEO DUFF, one of the attorneys for the plaintiffs-appellants herein, hereby certifies that on the 12th day of October, 1976, he caused the service of two copies of the within Brief upon EATON, VAN WINKLE & GREENSPOON, attorneys for the defendants-appellees herein, by depositing same in a securely sealed pre-paid envelope, and mailing same to 600 Third Avenue, New York, New York 10016, that being the address given by said attorneys in prior proceedings herein and in the Court below.

Dated: New York, New York
October 12, 1976



REGINALD LEO DUFF

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